Supreme Court, U.S.
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Nos. 00-568 AND 00-809

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

Enron Power Marketing, Inc.,
Petitioner,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOINT APPENDIX (Vol. 2 of 2)

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NOTICE

The following documents have been omitted in the printing of this Appendix. These documents may be found in Petitioner Enron Power Marketing, Inc.'s Appendix to its Petition for Writ of Certiorari (00-809) at the following pages:

APPENDIX A:

Judgment of the United States Court of Appeals for the District of Colombia Circuit filed 6/30/00 . . . . . 1a

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Some may also be found in the Petitioner's People of the State of New York and The Public Service Commission of the State of New York's Appendix to its Petition for Writ of Certiorari (00-568) at the following pages:

APPENDIX A:

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PART 35 - FILING OF RATE SCHEDULES
61 FED. REG. 21692-21695

1. The authority citation for part 35 continues to read as follows:

Authority: 16 U.S.C. 791a-825r, 2501-2645; 31 U.S.C. 9701; 42 U.S.C. 7101-7352,

2. Part 35 is amended by revising§35.15, by redesignating §35.28 as §35.29, and by adding new §§35.26, 35.27, and 35.28 to read as follows:

§35.15 Notices of cancellation or termination

(a) *General rule*. When a rate schedule or part thereof required to be on file with the Commission is proposed to be cancelled or is to terminate by its own terms and no new rate schedule or part thereof is to be filed in its place, each party required to file the schedule shall notify the Commission of the proposed cancellation or termination on the form indicated in §131.53 of this chapter at least sixty days but not more then one hundred-twenty days prior to the date such cancellation or termination is proposed to take effect. A copy of such notice to the Commission shall be duly posted. With such notice each filling party shall submit a statement giving the reasons for the proposed cancellation or termination, and a list of the affected purchasers to whom the notice has been mailed. For good cause shown, the Commission may by order provide that the notice of cancellation or termination shall be effective as of a date prior to the date of filing or prior to the date the filing would became effective in accordance with these rules.

(b) *Applicability*. (1) The provisions of paragraph (a) of this section shall apply to all contracts for unbundled transmission service and all power sale contracts:

(i) Executed prior to July 9,1998; or

(ii) If unexecuted, filed with the Commission prior to July 9, 1996.

(2) Any power sales contract executed on or after July 9, 1996 that is to terminate by its own terms shall not be subject to the provisions of paragraph (a) of this section.

(3) *Notice.* Any public utility providing jurisdictional services under a power sales contract that is not subject to the provisions of paragraph (a) of this section shall notify the Commission of the date of the termination of such contract within 30 days after such termination takes place.

§35.26 Recovery of stranded costs by public utilities and transmitting utilities.

(a) *Purpose.* This section establishes the standards that a public utility or transmitting utility must satisfy in order to recover stranded costs.

(b) *Definitions.*

(1) *Wholesale stranded cost* means any legitimate, prudent and verifiable cost incurred by a public utility or a transmitting utility to provide service to:

(i) A wholesale requirements customer that subsequently becomes, in whole or in part, an unbundled wholesale transmission services customer of such public utility or transmitting utility; or

(ii) A retail customer, or a newly created wholesale power sales customer, that subsequently becomes, in whole or in part, an unbundled wholesale transmission services customer of such public utility or transmitting utility.

(2) *Wholesale requirements customer* means a customer for whom a public utility provides by contract any portion of its bundled wholesale power requirements.

(3) *Wholesale transmission services* has the same meaning as provided in section 3(24) of the Federal Power Act (FPA): the transmission of electric energy sold, or to be sold, at wholesale in interstate commerce.

(4) *Wholesale requirements contract* means a contract under which a public utility or transmitting utility provides any portion of a customer's bundled wholesale power requirements.

(5) *Retail stranded costs* means any legitimate, prudent and verifiable cost incurred by a public utility or transmitting utility to provide service to a retail customer that subsequently becomes, in whole or in part, an unbundled retail transmission services customer of that public utility or transmitting utility.

(6) *Retail transmission services* means the transmission of electric energy sold, or to be sold, in interstate commerce directly to a retail customer.

(7) *New wholesale requirements contract* means any *wholesale requirements* contract extended after July 11, 1994, or extended or renegotiated to be effective after July 11, 1994.

(8) *Existing wholesale requirements* contract means any *wholesale requirements* contract executed on or before July 11, 1994.

(c) *Recovery of wholesale stranded costs.*

(1) *General requirement.* A public utility or transmitting utility will be allowed to seek recovery of wholesale stranded costs only as follows:

(i) No public utility or transmitting utility may seek recovery of wholesale stranded costs if such recovery is explicitly prohibited by a contract or settlement agreement, or by any power sales or transmission rate schedule or tariff.

(ii) No public utility or transmitting utility may seek recovery of stranded costs associated with a new wholesale requirements contract if such contract does not contain an exit fee or other explicit stranded cost provision.

(iii) If wholesale stranded costs are associated with a new wholesale requirements contract containing an exit fee or other explicit stranded cost provision, and the seller under the contract is a public utility, the public utility may seek recovery of such costs, in accordance with the contract, through rates for electric energy under sections 205-208 of the FPA. The public utility may not seek recovery of such costs through any transmission rate for FPA section 205 or 211 transmission services.

(iv) If wholesale stranded costs are associated with a new wholesale requirements contract, and the seller under the contract is a transmitting utility but not also a public utility, the transmitting utility may not seek an order from the Commission allowing recovery of such costs.

(v) If wholesale stranded costs are associated with an existing wholesale requirements contract, if the seller under such contract is a public utility, and if the contract does not contain an exit fee or other explicit stranded cost provision, the public utility may seek recovery of stranded costs only as follows:

(A) If either party to the contract seeks a stranded cost amendment pursuant to a section 205 or section 208 filing under the FPA made prior to the expiration of the contract, and the Commission accepts or approves an amendment permitting recovery of stranded costs, the public utility may seek recovery of such costs through FPA section 205-206 rates for electric energy.

(B) If the contract is not amended to permit recovery of stranded costs as described in paragraph (c)(1)(v)(A) of this

section, the public utility may file a proposal, prior to the expiration of the contract, to recover stranded costs through FPA section 205-206 or section 211-212 rates for wholesale transmission services to the customer.

(vi) If wholesale stranded costs ere associated with an existing wholesale requirments contract, if the seller under such contract is a transmitting utility but not also a public utility, and if the contract does not contain an exit fee or other explicit stranded cost provision, the transmitting utility may seek recovery of stranded costs through FPA section 211-212 transmission rates.

(vii) If a retail customer becomes a legitimate wholesale transmission customer of a public utility or transmitting utility, *e.g.*, through municipalization, and costs are stranded as a result of the retail-turned-wholesale customer's access to wholesale transmission, the utility may seek recovery of such costs through FPA section 205-206 or section 211-212 rates for wholesale transmission services to that customer.

(2) *Evidentiary demonstration for wholesale stranded cost recovery*. A public utility or transmitting utility seeking to recover wholesale stranded costs in accordance with paragraphs (c)(1)(v)-(vii) of this section must demonstrate that:

(i) It incurred stranded costs on behalf of its wholesale requirements customer or retail customer based on a reasonable expectation that the utility would continue to serve the customer;

(ii) The stranded costs are not more than the customer would have contributed to the utility had the customer remained a wholesale requirements customer of the utility, or, in the case of a retail-turned-wholesale customer, had the customer remained a retail customer of utility; and

(iii) The stranded costs are derived using the following formula: Stranded Cost Obligation -- (Revenue Stream Estimate- Competitive Market Value Estimate) x Length of Obligation (reasonable expectation period),

(3) *Rebuttable presumption.* If a public utility or transmitting utility seeks recovery of wholesale stranded costs associated with an existing wholesale requirements contract, as permitted in paragraph (c)(1) of this section, and the existing wholesale requirements contract contains a notice provision, there will be a rebuttable presumption that the utility had no reasonable expectation of continuing to serve the customer beyond the term of the notice provision.

(4) *Procedure for customer to obtain stranded cost estimate.* A customer under an existing wholesale requirements contract with a public utility seller may obtain from the seller an estimate of the customer's stranded cost obligation if it were to leave the public utility's generation supply system by filing with the public utility a request for an estimate at any time prior to the termination date specified in its contract.

(i) The public utility must provide a response within 30 days of receiving the request. The response must include:

(A) An estimate of the customer's stranded cost obligation based on the formula in paragraph (c)(2)(iii) of this section;

(B) Supporting detail indicating how each element in the formula was derived;

(C) A detailed rationale justifying the basis for the utility's reasonable expectation of continuing to serve the customer beyond the termination date in the contract;

(D) An estimate of the amount of released capacity and associated energy that would result from the customer's departure; and

(E) The utility's proposal for any contract amendment needed to implement the customer's payment of stranded costs.

(ii) If tim customer disagrees with the utility's response, it must respond to the utility within 30 days explaining why it disagrees. If the parties cannot work out a mutually agreeable resolution, they may exercise their rights to Commission resolution under the FPA.

(5) A customer must be given the option to market or broker a portion or all of the capacity and energy associated with any stranded costs claimed by the public utility.

(i) To exercise the option, the customer must so notify the utility in writing no later than 30 days after the public utility files its estimate of stranded costs for the customer with the Commission.

(A) Before marketing or brokering can begin, the utility and customer must execute an agreement identifying, at a minimum, the amount and the price of capacity and associated energy the customer is entitled to schedule, and the duration of the customer's marketing or brokering of such capacity and energy.

(ii) If agreement over marketing or brokering cannot be reached, and the parties see Commission resolution of disputed issues, upon issuance of a Commission order resolving the disputed issues, the customer may reevaluate its decision in paragraph (c)(5)(i) of this section to exercise the marketing or brokering option. The customer must notify the utility in writing within 30 days of issuance of the Commission's order resolving the disputed issued whether the customer will market or broker a portion or all of the capacity and energy associated with stranded costs allowed by the Commission.

(iii) If a customer undertakes the brokering option, and the customer's brokering efforts fail to produce a buyer within 60 days of the date of the brokering agreement entered into between the customer and the utility, the customer shall relinquish all rights to broker the released capacity and associated energy and will pay stranded costs as determined by the formula in paragraph (c)(2)(iii) of this section.

(d) *Recovery of retail stranded costs.*

(1) *General requirement.* A public utility may seek to recover retail stranded costs through rates for retail transmission services only if the state regulatory authority does not have authority under state law to address stranded costs at the time the retail wheeling is required.

(2) *Evidentiary demonstration necessary for retail stranded cost recovery.* A public utility seeking to recover retail stranded costs in accordance with paragraph (d)(1) of this section must demonstrate that:

(i) It incurred stranded costs on behalf of a retail customer that obtains retail wheeling based on a reasonable expectation that the utility would continue to serve the customer; and

(ii) The stranded costs are not more than the customer would have contributed to the utility had the customer remained a retail customer of the utility.

§35.27 Power sales at market-based rates.

(a) Notwithstanding any other requirements, any public utility seeking authorization to engage in sales for resale of electric energy at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity for which construction has commenced on or after July 9, 1996.

(b) Nothing in this part

(1) Shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or

(2) Limits the authority of a state commission in accordance with state and federal law to establish

(i) Competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or

(ii) Non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

§35.28 Non-discriminatory open access transmission tariff.

(a) *Applicability*. This section applies to any public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce and to any nonpublic utility that seeks voluntary compliance with jurisdictional transmission tariff reciprocity conditions.

(b) *Definitions*.

(1) *Requirements service agreement* means a contract or rate schedule under which a public utility provides any portion of a customer's bundled wholesale power requirements.

(2) *Economy energy coordination agreement* means a contract, or service schedule thereunder, that provides for trading of electric energy on an "if, as require either the seller or the buyer to engage in a particular transaction.

(3) *Non-economy energy coordination agreement* means any non-requirements service agreement, except an economy energy coordination agreement as defined in paragraph (b)(2) of this section.

(c) *Non-discriminatory open access transmission tariffs.*

(1) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce must have on file with the Commission a tariff applicability for transmission services, including ancillary services, over such facilities. Such tariff must be the open access pro forma tariff contained in Order No. 888. FERC Stats. & Regs. ¶31,036 (Final Rule on Open Access and Stranded Costs) or such other open access tariff as may be approved by the Commission consistant with Order No. 888, FERC Stats. & Regs. ¶31,036.

(i) Subject to the exceptions in paragraphs (c)(1)(ii), (c)(1)(iii), and (c)(1)(iv) of this section, the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, and accompanying rates, must be filed no later than 60 days prior to the data on which a public utility would engage in a sale of electric energy at wholesale in interstate commerce or in the transmission of electric energy in interstate commerce.

(ii) If a public utility owns, controls or operates facilities used for the transmission of electric energy in interstate commerce as of July 9, 1996, it must file the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, pursuant to section 206 of the FPA and accompanying rates pursuant to section 205 of the FPA, no later than July 9, 1996. However, if a public utility has already filed, or has on file, an open access tariff and accompanying rates as of April 24, 1996, it may, but is not required to, file new rates with its section 206 pro forma tariff filing.

(iii) If a public utility owns, controls or operates transmission facilities used for the transmission of electric energy in interstate commerce as of July 9, 1996, such

facilities are jointly owned with a non-public utility, and the joint ownership contract prohibits transmission service over the facilities to third parties, the public utility with respect to access over the public utility's share of the jointly owned facilities must file no later than December 31, 1996 the pro forma tariff contained in Order No. 888, FERC Stats. & Regs. ¶31,036, pursuant to section 206 of the FPA and accompanying rates pursuant to section 205 of the FPA.

(iv) If a public utility obtains a waiver of the tariff requirement pursuant to paragraph (d) of this section, it does not need to file the pro forma tariff required by this section.

(v) Any public utility that seeks a deviation from the pro forma tariff combined in Order No. 888, FERC Stats. & Regs. ¶31,036, must demonstrate is consistent with the principles of Order No. 888, FERC Stats. & Regs. ¶31,036.

(2) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce, and tat used those facilities to engage in wholesale sales and/or purchases of electric energy, or unbundled retail sales of electric energy, must take transmission service for such sales and/or purchases under the open access tariff filed pursuant to this section.

(i) Subject to the exceptions in paragraphs (c)(2)(ii) and (c)(3)(iv) of this section, this requirement is effective on the date that such public utility engages in a wholesale sale or purchase of electric energy, but no earlier than July 9, 1996.

(ii) For sales of electric energy pursuant to a requirements service agreement executed on or before July 9, 1996, this requirement will not apply unless separately ordered by the Commission. For sales of electric energy pursuant to a bilateral economy energy coordination agreement executed on or before July 9, 1996, this requirement is effective on December 31, 1996. For sales of

electric energy pursuant to a bilateral non-economy energy coordination agreement executed on or before July 9, 1996, this requirement will not apply unless separately ordered by the Commission.

(2) Every public utility that owns, controls or operates facilities used for the transmission of electric energy in interstate commerce, and that is a member of a power pool, public utility holding company, or other multi-lateral trading arrangement or agreement that contains transmission rates, terms or conditions, must file a joint pool-wide or system-wide open access transmission pro forma tariff.

(i) For any power pool, public utility holding company, or other multi-lateral trading arrangement or agreement that contains transmission rates, terms or conditions and that is executed after July 9, 1996, this requirement is effective on the date that transactions begin under the arrangement or agreement.

(ii) For any public utility holding company arrangement or agreement that contains transmission rates, terms or conditions and that is executed on or before July 9, 1996, this requirement is effective July 9, 1996, except for the Central and South West System, which must comply no later than December 31, 1996.

(iii) For any power pool or multilateral arrangement or agreement other than a public utility holding company arrangement or agreement, that contains transmission rates, terms or conditions and that is executed prior to July 9, 1996, this requirement is effective on December 31, 1996.

(iv) A public utility member of a power pool, public utility holding company or other multi-lateral arrangement or agreement that contains transmission rates, terms or conditions and that is executed on or before July 9, 1996 must begin to take service under a joint pool-wide or system-wide

pro forma tariff for wholesale trades among the pool or system members no later than December 31, 1996.

(d) *Waivers*. A public utility subject to the requirements of this seciion and Order No. 889, FERC Stats. & Regs. ¶31,037 (Final Rule on Open Access Same-Time Information System and Standards of Conduct forPublic Utilities) may file a request for waiver of all or part of the requirements of this section, or Part 37 (Open Access Same-Time Information System and Standards of Conduct for Public Utilities), for good cause shown. An application for waiver must be filed either:

(i) No later than July 9, 1996 or

(ii) No later than 60 days prior to the time the public utility would otherwise have to comply with the requirement.

(e) *Non-public utility procedures for tariff reciprocity compliance*.

(1) A non-public utility may submit a transmission tariff and a request for declaratory order that its voluntary transmission tariff meets the requirements of Order No. 888 (Final Rule on Open Access and Stranded Costs).

(i) Any submittal and request for declaratory order submitted by a non-public utility will be provided an NJ (non-jurisdictional) docket designation.

(ii) If the submittal is found to be an accceptable transmission tariff, an applicant in a Federal Power Act (FPA) section 211 case against the non-public utility shall have the burden of proof to show why service under the open access tariff is not sufficient and why a section 211 order should be granted.

(2) A non-public utility may file a request for waiver of all or part of the reciprocity conditions contained in a public utility open access tariff, for good cause shown. An application for waiver may be filed at any time.

PENNSYLVANIA PUBLIC UTILITY COMMISSION'S PETITION FOR REHEARING

[pp. 1-2]

[1]

UNITED STATES OF AMERICA FEDERAL REGULATORY COMMISSION

[May 23, 1996]

Docket Nos. RM95-8-000 and RM94-7-001

Promoting Wholesale Competition	)
Open Access Non-discriminatory	)
Transmission Services by Public	)
Utilities	)
	)
Recovery of Stranded Costs by	)
Public Utilities and Transmitting	)
Utilities	)
	)

PENNSYLVANIA PUBLIC UTILITY COMMISSION
PETITION FOR REHEARING

BEFORE THE FEDERAL ENERGY REGULATORY COMMISSION:

The Pennsylvania Public Utility Commission ("PaPUC") is the state agency responsible for regulating the rates and service for all privately owned distribution companies and utilities providing electric services within the Commonwealth of Pennsylvania. The PaPUC hereby petitions the Federal Energy Regulatory Commission ("Commission"

or "FERC") for rehearing and reconsideration of its Order No. 888 and the related Final Environmental Impact Statement issued in the above-captioned proceeding consistent with 16 U.S.C. §8251. Specifically, the PaPUC is concerned with the following issues:

Open Access Issues

Issue No. 1 The FERC Has Exceeded the Scope of its Statutory Authority by Requiring Generic Unbundling, Open Access, and Comparability Under Order No. 888.

Issue No. 2 The FERC's Curtailment Policy on a Pro-rata Basis Fails to Hold the Native Load Harmless, "to the extent practical," as Required under the Federal Power Act.

[2]

Issue No. 3 The Redefinition of Federal and State Jurisdiction Under the FERC'S Technical/Functional Test and the Seven Indicia of Distribution are contrary to Law and Fact. (See, Order No. 888 Mimeo at pages 401-443, and Appendix G)

* * * * *

[pp. 18-35]

[18]

Issue No. 2 The FERC's Curtailment Policy on a Pro-rata Basis Fails to Hold the Native Load Harmless, "to the extent practical," as Required under the Federal Power Act.

Under Order No. 888, the transmission provider has the discretion to curtail services, whether firm or non-firm, that will substantially relieve a constraint. That curtailment must be made on a non-discriminatory basis, including the transmission provider's own use of the system, and thus by implication service to the native load.Curtailment must be pro-rata. See, Order No. 888 Mimeo page 335.

While many aspects of the curtailment queue set forth in Order No. 888 are logical, this blanket pro-rata curtailment requirement sets up utility native loads for curtailment while regional, wholesale economic transactions continue to take place. While state curtailment priorities in place, there will already have been a curtailment at the regional level affecting the transmission provider's own use of the system. As part of that use must be to serve the native load, those core customers for whom the system was originally built and maintained under the regulatory compact will be impacted. The degree of those impacts will depend upon the extent and duration of the constraint and the time of day, **[19]** season and climatic conditions under which curtailment takes place.

The PaPUC is particularly aware of this problem in light of experience on January 19, 1994, when pro-rata load shedding was initiated by the Pennsylvania-New Jersey-Maryland Interconnection, in part to preserve economic transactions. As a result, core customers in Pennsylvania ranging from neighborhoods to entire municipalities were abruptly left without power during a record cold spell.

Issue No. 3 The Redefinition of Federal and State Jurisdiction Under the FERC's Technical/Functional Test and the Seven Indicia of Distribution are Contrary to Law and Fact. (See, Order No. 888 Mimeo at pages 401-443, and Appendix G)

Summary

While this issue is presented in the order in which it appears in Order No. 888, it is actually the priority issue for the PaPUC. While specific page cites to the Mimeo Order No. 888 will be provided, the PaPUC also offers a summary of this core issue taken from its Comments and Reply Comments to the MegaNOPR.

> At Order No. 888 Mimeo page 432, the FERC asserts that:
>
> The Commission's assertion of jurisdiction is that if retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

Order No. 888, Mimeo at page 432.

The PaPUC is very concerned with respect to the possibility of a "chilling,, of the development of retail

competition given the **[20]** litigation that may attend the FERC's expansive view of jurisdiction over what it terms, "retail transmission,"[18] and "local distribution." The FERC's declaration of jurisdiction over the rates, terms and conditions of retail wheeling service once that service has been ordered or allowed by a state commission creates a powerful disincentive to authorize or to allow retail wheeling. That is inimical to the evolution of a competitive electric industry and threatens to precipitate extensive litigation with respect to jurisdiction.

The FERC's jurisdiction is much more limited than described in Order No. 888. It extends only to wholesale power transmission and transactions. The FERC does not have the authority to order retail wheeling. Further, the PaPUC does not accede to the jurisdictional formula for determining, "interstate transmission," propounded in the NOPR. That formula may be challenged both on engineering and legal grounds.

The PaPUC does not agree, as a matter of law, that the FERC has jurisdiction over what it terms, the rates, terms and conditions of service of unbundled interstate retail transmission service. The PaPUC disagrees with the FERC's

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[18]Retail transmission services, as defined by the FERC, means the transmission of electric energy sold, or to be sold, in interstate commerce directly to a retail customer. NOPR Mimeo, page 310. PaPUC maintains that unless a state has authorized retail wheeling, there can be no sale of electricity in interstate commerce to a retail customer. Even if retail wheeling is authorized the sale of electricity will, most likely, be a function of intrastate commerce.

claim that the "plain meaning," of the Federal Power Act supports this contention. Just **[21]** because there is nothing in the statute, the legislative history, or the case law to indicate that the FERC's jurisdiction over the rates, terms and conditions of transmission in interstate commerce extends only to wholesale transmission and not to retail transmission, that does not amount to a grant of jurisdiction over what are retail services.

With the exception of a change in customer status caused by municipalization, PaPUC challenges both the FERC's attempt to take jurisdiction over retail wheeling and retail stranded costs cases as well as the concept of, "transmission at retail in interstate commerce," or "retail transmission." If a state has not approved wheeling to retail customers, then there is no legal basis for the transaction even to take place.

With respect to the FERC's analysis of jurisdictional facilities and line-drawing between transmission and distribution plant, the PaPUC agrees that the Federal Power Act and case law supports the conclusion that facilities of a public utility used to deliver electric energy in interstate commerce to a wholesale purchaser are subject to the FERC's jurisdiction. Whether such facilities are labeled "transmission," "distribution" or ,local distribution," makes a great deal of difference, however, as the United States Supreme Court made clear in the key case of Connecticut Light & Power Company v. Federal Power Commission,[19] In that case, the United States Supreme Court interpreted the

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[19]Id.

Federal Power Act's Section 201(b) local distribution provision, **[22]** effectively dismissing the very sort of, "negative authority," and combined technical-functional arguments for federal jurisdiction made by the FERC throughout the MegaNOPR and Order No. 888.

The FERC proposes technical factors to evaluate whether particular facilities are transmission or local distribution facilities in the case of vertically integrated transmission and distribution utilities. Those seven indicia of distribution are neither accurate nor acceptable measures of local distribution.

The FERC contends at page 282 of the MegaNOPR and page 403 of the order No. 888 Mimeo that there are seven indicia of local distribution. While advancing the offer of deference to state determinations of what constitutes distribution, the FERC requires the application of the seven indicia by the states in making those determinations. See, Order No. 888 Mimeo at page 430. PaPUC will list those indicia and explain why they are not acceptable measures of local distribution:

1. Local distribution facilities are normally in close proximity to retail customers.

The definition of, "in close proximity," is manifestly unclear and a fertile ground for litigation. By this indicia, the very retail customers that take service at high voltage from transmission lines might be viewed as rendering those lines local distribution facilities by virtue of their close proximity to a retail customer.

[23]

2. Local distribution facilities are primarily radial in character.

Electric distribution may be "radial in character," because the physics of the system as originally constructed dictated that arrangement. But distribution is not always radial in character, nor do the physics of the system require that the system be radial in character. There is no jurisdictional magic in the radial character of distribution lines. Distribution circuits are often networked or looped with adjacent distribution circuits for reliability and load shifting purposes. On the other hand, distribution lines in rural areas are often radial because the circuits are not in close enough proximity to be looped or networked. In short, the radial character of a distribution system (or the lack of same) is not an indicia of local distribution.

3. Power flows into local distribution systems, it rarely, if ever, flows out.

Again, this is a rather gross oversimplification of an engineering concept. All electric power flows out from generators and into the transmission and distribution systems. This concept is dispositive of nothing, including jurisdictional arguments. Whatever power load a circuit cannot absorb goes elsewhere, i.e. it, "flows out."

[24]

4. When power enters a local distribution system, it is not reconsigned or transported on to some other market.

Nor is power reconsigned or transported on to some other market on the transmission grid. This indicia points up the FERC's fundamental failure to understand the dramatically different physics of the electric transmission system. Unlike gas pipelines, which can be packed with molecules that are directed along a closed system, energy transmission is a function of generator location and power displacement. Electric energy is not consigned or transported. Generation and transmission assets are used to increase capacity in a particular area to accommodate coordinated generation and transmission from other areas. Unlike natural gas, there is simply no way to, "paint" an electron a particular color, and to track it from the west to its ultimate destination in the east. Electrons do not move in that fashion. The FERC is confusing consignment and transportation with energizing the grid.

5. Power entering a local distribution system is consumed in a comparatively restricted geographical area.

Again, this indicia is not dispositive of the jurisdictional question. All power is consumed in restricted geographical areas. The electrons leaving a generation plant in Ohio are not the same electrons that arrive in New York.

[25]

6. Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

Meters can be, and often are, installed at many points within the power grid as part of a utility's telemetry system

for monitoring the performance of its system. This indicia does not resolve jurisdictional issues but merely reflects a physical manifestation of economic and reliability requirements.

7. Local distribution systems will be of reduced voltage.

In footnote 396 which refers to this indicia, the FERC states:

> The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.

This generalization is not helpful in resolving the jurisdictional issue, because local distribution can and does occur at levels both higher and lower than those provided by the FERC. Distribution to light industry can occur at 69 kY. Advances in the state of the art now allow a retail residential single phase customer to be served directly from a 34 kV line. Twenty-five years ago, this customer would typically have been served from a 4.16 kV distribution circuit. Does the FERC propose to continue to re-draw its jurisdictional line, periodically, based on technological advances?

Note that regardless of what line of case-law the parties follow, whether AGD or CL&P, the FERC itself states in Order No. **[26]** 888 that, ". . . the cases simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry." Order No. 888 Mimeo at page 429.

Nothing set forth in Order No. 888, save an as yet undefined offer of deference to state authorities which will be discussed below, changes the positions of the FERC or the PaPUC which have been consistent from July, 1994, when the FERC first articulated its new jurisdictional theories in the original Stranded Cost NOPR.[20]

The PaPUC offers its further assessment of the FERC's jurisdictional theory as articulated in Order No. 888. Eligibility to receive unbundled transmission service is not limited to wholesale customers under Order No. 888. The FERC contends: "It is irrelevant to the Commission's jurisdiction whether the customer receiving the unbundled transmission service in interstate commerce is a wholesale or retail customer." See, Order No. 888 Mimeo page 157. Given the fundamental disagreement with the FERC's jurisdictional theories as finalized in Order No. 888, this contention cannot be allowed to stand. To the PaPUC, it is quite relevant whether a customer is receiving wholesale or retail service. Redefining transmission and distribution service as the FERC

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[20] F.E.R.C. Docket No. RM94-7-000, Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, 67 F.E.R.C. ¶61,394 (1994).

does in Order No. 888 does not automatically convey jurisdiction to the FERC, particularly as that redefinition is **[27]** based on an approach specifically rejected by the United States Supreme Court in Connecticut Light & Power Company v. Federal Power Commission.[21]

The PaPUC disagrees as a matter of law with the FERC's assertion that the FERC has exclusive jurisdiction over what it has defined as, "retail transmission." See, Order No. 888 Mimeo page 401. The FERC is impermissibly attempting to expand its jurisdiction, not by virtue of new statutory authority, but by an impermissibly broad and technically insupportable re-definition of existing statutory authority. If it was the intent of Congress to do something so substantial as to redefine and to restructure the electric industry as is argued by the FERC, that intent would be explicit and would not have to be interpreted. In this respect, witness the hearings held before both the U.S. House Energy and Power Subcommittee and the U.S. Senate Energy and Natural Resources Committee thus far on 1996. Those hearings have repeatedly raised the question, both expressly and impliedly, as to whether the FERC has the requisite statutory authority to restructure the electric industry. If the Congress, which the FERC consistently points to as having mandated industry restructuring, must ask such questions then it is questionable whether the FERC's interpretation of the scope of the Energy Policy Act Amendments and the will of Congress is correct.

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[21]324 U.S. 515, 65 S.Ct. 749, 89 L.Ed. 1150 (1945).

The PaPUC questions the seven indicia of distribution proposed by the FERC on the basis of both fact and law as stated, above. **[28]** See, Order No. 888 Mimeo page 403.

The PaPUC questions as a matter of law the FERC's definition of the, "traditional tasks of state and federal regulators." See, Order No. 888 Mimeo pages 428-429, See also, fn 541 at p. 431, fn. 544 at p. 435. At the heart of this issue is a fundamental difference with respect to the interpretation of Section 201(b) of the Federal Power Act, the Supremacy Clause, and the X Amendment of the United States Constitution.

FERC Deference to the States

The PaPUC requests clarification of the concept of deference to the states in the definition of local distribution services as first articulated in Order No. 888. The FERC announces this deference at several points in the order, but the FERC does not clarify what a state regulatory agency must demonstrate to secure deference. Further, the FERC offers utilities the opportunity to initiate jurisdictional determinations, by the FERC, regardless of what a state might do. It is only required that a utility first, "consult," with a state prior to coming to the FERC for a jurisdictional determination, and the nature of that, "consultation," is undefined. The language of Order No. 888 also poses a problem for those states contemplating retail wheeling in that deference requires the application of the seven indicia of distribution and conclusions consistent with the findings of Order No. 888:

[29]

> Determining where to draw the jurisdictional line for facilities used in unbundled retail wheeling transactions will involve case-specific determinations that evaluate the seven local distribution indicators that we are adopting. We believe that the Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate. Therefore, in instances of unbundled retail wheeling that occurs as a result of a state retail access program, we will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[[548] Footnote in Order No. 888] Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by

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[548]In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.

> states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Order 888 Mimeo at pages 438-439.

This deference provision appears, on its face, only to grant deference in those cases where a state implements the FERC's seven indicia of local distribution and the balance of the open access and comparability portions of the order as stated. Of greater importance to the states are the final two sentences of the quote, above:

[30]

> Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Order No. 888 Mimeo at page 439.

Note well that variations from the seven indicia of distribution are not deferred to; they are subject to the FERC's consideration. This is a critical distinction that requires elaboration by the FERC.

Given the crucial difference between, "deference" and "consideration," it is clear that under Order No. 888 any state

that authorizes or allows retail wheeling faces the risk of attempted federal preemption by the FERC. The extent of that risk, and the efficacy of the undefined vehicle for FERC, "consideration" of state jurisdictional recommendations beyond the seven indicia of distribution remain unknown.

FERC Resolution of Jurisdictional Issues Initiated by Utilities

Equally troubling is what might be construed as the FERC's attempt to set itself up as a de facto appellate authority should a utility, "consult" with its state regulator but then go to the FERC for a jurisdictional determination. Carefully consider the following language from Order No. 888:

[31]

> Some commenters have asked the Commission to provide a forum to prevent or resolve disputes over the correct classification of facilities as transmission or local distribution. As a means of facilitating jurisdictional line-drawing, we will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with

> the principles established in the Final Rule, the Commission will defer to such classifications and/or cost allocations. [footnote deleted] We encourage public utilities and their state regulatory authorities to attempt to agree to utility-specific classifications and allocations that the utility may file at the Commission.

Order No. 888 Mimeo at 439-440 (emphasis added)

This section of Order No. 888 appears to leave the door open to utilities to circumvent the statutory authority of state regulators. It is not clear what the FERC will do if a utility's classifications and/or cost allocations are <u>not</u> supported by state regulatory authorities. This must be clarified.

<u>FERC Assertion of Jurisdiction Over the Rates, Terms and Conditions of, "Unbundled Retail Transmission."</u>

In its Comments and Reply Comments to the MegaNOPR, the PaPUC challenged the FERC's assertion of jurisdiction over what it terms, "retail transmission." The FERC has reiterated that jurisdictional claim in Order No. 888. In this area, the FERC also speaks of, "deference" to state regulators:

[32]

> A number of commenters have asked the Commission to defer to state commission recommendations or decisions regarding rates, terms and conditions of unbundled retail transmission in interstate commerce by public utilities. Some have suggested that we set

> broad guidelines for such rates, terms, and conditions, and then allow states to actually implement the guidelines. While the Commission cannot simply turn over its jurisdiction for the states to implement, we understand the concerns raised by many state regulators and believe that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances, as discussed below.
>
> As we determined in the NOPR, when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes - - a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the local distribution component. [[550] Footnote in Order No. 888] Thus, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of

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[550] As discussed above, even if there were instances where no local distribution facilities are used, we believe states have authority over the service of delivering electric energy to end users.

> a state retail access program, it may be appropriate to have a separate retail transmission tariff [[551] Footnote in Order No. 888] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing Policy Statement, and the guidance herein concerning ancillary **[33]** services. [[552] Footnote in Order No. 888]

Order No. 888 Mimeo at pages 440-441 (emphasis added)

The extent of, "deference" under this statement is undefined and is, perhaps, unknowable outside of specific proceedings. The PaPUC does not accept the FERC's claim of jurisdiction over, "retail transmission," and consequently must challenge the FERC's pronouncement of jurisdiction over the rates, terms and conditions of such service.

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[551] I.e., the tariff would be different from the tariff that applies to wholesale customers. Such tariff would still be filed with the Commission under FPA section 205.

[552] In applying the principles of the Final Rule to retail transmission tariffs, the Commission clearly cannot order retail wheeling directly to an ultimate consumer. See FPA section 212(h).

Buy-sell Transactions

In the MegaNOPR, the FERC discussed buy-sell transactions as a potential threat to FERC jurisdiction. That discussion is reiterated in Order No. 888:

> A final jurisdictional issue raised in the Open Access NOPR concerns buy-sell transactions. We remain concerned, just as we were with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, we reaffim our conclusion that we have jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. However, we recognize that there is a wide range of programs and transactions that might or might not fall within this category. We will address these on a case-by-case basis.

Order No. 888 at page 442

[34]
Again, there is a potential for a jurisdictional conflict with respect to buy-sell transactions to end users that are retail end users. This is a direct consequence of the FERC's "technical-functional test" for jurisdiction. That test is challenged by the PaPUC on legal and technical grounds as described, above.

Conclusion and Summary of the Jurisdictional Section of Order No. 888

The PaPUC renews its objection to the jurisdictional theories of the FERC as summarized at pages 442-443 of Order No. 888:

> In summary, the Commission reaffirms and clarifies its prior jurisdictional conclusions and tests for determining the demarcation between federal and state jurisdiction over transmission in interstate commerce and local distribution. We have attempted to address these issues in a way that provides for flexibility and recognition of legitimate state concerns. With regard to retail services, we recognize the states' concerns that the unbundling of retail transactions would result in changes from what historically has been regulated by the states (principally, the rates of transmission assets previously included in retail rate base). However, the decision to provide unbundled retail wheeling is not the Commission's to make because we have no authority to order transmission directly to an ultimate consumer. In addition, even if a retail access program occurs, we do not believe the unbundling of retail transactions will radically change fundamental state authorities, including authority to regulate the vast majority of generation asset costs, the siting and maintenance of generation facilities and transmission lines, and decisions regarding

> retail service territories. Further, the Commission intends to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies. As the electric industry and state regulatory authorities continue to develop new competitive market structures and consider retail wheeling programs, we believe that the tests and mechanisms we have provided in this Rule will accommodate both Federal and state interests and will help provide jurisdictional certainty to market participants.

[35]
Order No. 888 Mimeo at pages 442-443 (emphasis added)

The PaPUC views with concern the tacit admission by the FERC that assets previously included in retail rate base will be effectively removed from that rate base by virtue of the FERC's re-definition of, "transmission." As those assets were, most likely, previously reviewed and approved by state regulators and form an intrinsic part of state-jurisdictional utility rate base, it is unacceptable for the FERC unilaterally to attempt to wrest jurisdiction from the states. Whether or not one agrees with the regulatory compact and traditional rate-making, the fact remains that the transmission assets previously included (and still included) in retail ratebase are in that rate base as a result of statute. FERC can point to no law that allows it to take jurisdiction of these assets. The inherent and historic nature and use of these facilities by state jurisdictional utilities and their core retail customers virtually

compels state defense of its jurisdiction lest the core of that jurisdiction be undermined.

REQUEST OF THE STAFF OF THE VIRGINIA STATE CORPORATION COMMISSION FOR REHEARING

[p. 1]

United States of America
Federal Energy Regulatory Commission

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities	)
Recovery of Stranded Costs by Public Utilities and Transmitting Utilities	)

Docket Nos. RM95-8-001 and RM94-7-002

REQUEST OF THE STAFF OF THE VIRGINIA STATE CORPORATION COMMISSION FOR REHEARING

The Staff of the Virginia State Corporation Commission ("VSCC Staff"), pursuant to Rule 713 of the commission's Rules of Practice and Procedure, 18 C.F.R. 385.713, hereby requests rehearing of the Commission's Order No. 888 issued in the above-captioned proceeding on April 24, 1996. Order 888 is unlawful or improper for the following reasons:

1. FERC exceeded the scope of its statutory authority by requiring generic industry-wide unbundling, open access, and comparability.

2. FERC's finding of industry-wide undue discrimination is not supported by the record.

3. FERC's assertion of jurisdiction over the rates, terms and conditions of unbundled retail transmission services is contrary to law.

4. FERC's assertion of jurisdiction over stranded costs related to retail wheeling is contrary to law.

5. FERC's assertion of jurisdiction over stranded costs from retail-turned-wholesale customers is contrary to law.

* * * * *

[pp. 3-9]

[3]

3. FERC's assertion of jurisdiction over the rates, terms and conditions of unbundled retail transmission services is contrary to law.

In Order 888, FERC asserts that "it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities." FERC also asserts that "it is irrelevant to the Commission's jurisdiction whether the customer receiving the unbundled transmission service in interstate commerce is a wholesale or retail customer." However, FERC cannot point to any specific legal authorization for such jurisdiction, and in fact admits that the law is not clear on this issue. This ambiguity should not be resolved in favor of expanding FERC's jurisdiction.

VSCC Staff agrees with FERC that the law is not dispositive on the question of unbundled retail transmission services. Section 201(a) of the FPA gives FERC **[4]** jurisdiction over ". . . the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce." Cases interpreting the FPA have not addressed the question of whether FERC's jurisdiction over transmission extends to retail customers.[1] However, one court expressly applied the wholesale versus retail distinction to distinguish transmission and local distribution.[2] FERC should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

The legislative history of the FPA does not resolve this jurisdictional question and it provides little support for FERC's conclusion that the act of unbundling generation from delivery shifts jurisdiction from a state to FERC. If anything, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. When Congress enacted the Energy Policy Act of 1992 (EPAct"), it reaffirmed the wholesale/retail distinction. It amended Section 212 of the FPA to prohibit FERC from issuing orders that require transmission of electric energy to a retail consumer, or that are otherwise inconsistent with state-regulated retail marketing

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[1]Jersey Central Power & Light Co. V. FPC, 319 U.S. 61 (1943); FPC v. Southern California Edison Co., 3876 U.S. 205 (1964); Arkansas Electric Cooperative Corp. V. Arkansas Public Service Commission, 461 U.S. 375 (1983).

[2]Wisconsin-Michigan Power Co. V. FPC, 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953).

areas of electric utilities. Further, Section 212(h) of the EPAct includes a provision protecting state authority "concerning the transmission of electric energy directly to an ultimate consumer" from interference by FERC's newly-expanded authority to order wholesale transmission services.

FERC should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to state jurisdiction, regardless of **[5]** the identity of the party generating or reselling the power or the facilities used to transport the power. This clarification of jurisdiction over delivery of third-party power to an end-user would promote FERC's competitive goals, and it would facilitate state retail wheeling programs that would have otherwise been hindered by Order 888's jurisdictional uncertainty.

4. FERC's assertion of jurisdiction over stranded costs related to retail wheeling is contrary to law.

A state, not FERC, has exclusive jurisdiction over any costs incurred on behalf of a retail customer. In Order 888, FERC asserts that a retail customer who leaves its native utility and takes retail service from an alternative supplier has crossed into the threshold of FERC jurisdiction. This has no basis in law, given the clear restriction on FERC's jurisdiction set forth in the FPA. Section 201(b)(1) restricts FERC's jurisdiction to wholesale sales, and explicitly excludes "any other sale of electric energy." A departing retail customer remains a retail customer, regardless of supplier. No portion of the transaction is a wholesale sale, and there are no wholesale costs associated with a retail

wheeling transaction. Therefore, FERC has no valid claim to address stranded costs arising from retail wheeling.

5. FERC's assertion of jurisdiction over stranded costs from retail-turned-wholesale customers is contrary to law.

Like its assertion of jurisdiction over stranded costs related to retail wheeling, FERC asserts that stranded costs arising from retail-turned-wholesale transactions are subject to FERC's jurisdiction. A change in a customer's status from retail to wholesale (e.g. through municipalization) does not change the status of historical costs. Costs **[6]** incurred on behalf of retail customers are subject to state jurisdiction. Whether a retail customer becomes a retail or wholesale customer of another utility is irrelevant for jurisdictional purposes. Any stranded costs associated with either transaction are costs incurred on behalf of a retail customer. The costs cannot be considered wholesale or transmission (thus FERC-jurisdictional) costs. Thus, there is no legal basis for FERC jurisdiction.

6. The reservation and curtailment priorities in the pro forma tariff fail to protect native load customers, who have paid for the existing transmission system.

Order 888 does not adequately protect native load customers. Native load customers have paid a large portion of the costs of the existing transmission system, and they have endured the environmental and aesthetic impacts associated with transmission lines. They depend on the utility, and unreliable service harms them. Native load customers should

be first in line to receive reserved transmission capacity and last in line to be curtailed in the event of a system constraint. The reservation and curtailment priorities established in Order 888 provide inadequate protection to native load. There are ambiguities in the Order that could be resolved in favor of economic transactions, to the detriment of native load.

A. Reservation Priority

Reservation priority establishes the order in which customers can obtain service. Order 888 allows utilities to reserve existing transmission capacity needed for native load growth and network load growth reasonably forecasted within the utility's current planning horizon. Any capacity reserved for future growth that is not currently needed [7] must be posted on the OASIS and made available to others until it is actually needed and used. Further, the Order gives existing firm customers a right of first refusal to existing capacity beyond the terms of their contracts, if they match the rate and contract length offered by another potential customer.

The Order gives native load customers some assurance that they will be entitled to receive service and that sufficient capacity will be reserved for them. However, forecasting load growth and calculating the amount of available transmission capability ("ATC") will be imprecise, at best. Forecasts of transmission load growth are more uncertain than forecasts for generation-related capacity requirements because such forecasts must predict where electrical demands will occur in addition to the magnitude of those loads. Calculations of ATC will be subject to uncertainties associated with load growth, load factors, generating unit availabilities, generating unit additions and retirements, economic

conditions, anomalies in weather, and numerous other factors. Further, in the past, utilities cooperated readily in transmission planning and construction. Under FERC's scheme, they will potentially be competitors and will be less likely to disclose their plans to each other. It will be very difficult, if not impossible, to determine the actual ACT on the transmission grid over both the long and short terms. Further complicating matters is the fact that FERC did not establish any specific method for calculating ATC, and instead will require utilities to file their own methods for calculating ATC.

The possibility that non-native customers could reserve capacity over the economic and reliability needs of native load customers is similar to problems associated **[8]** with the avoided costs provisions of PURPA, where third party power producers were able to enter into long-term purchased power contracts that were based on projections of needed capacity and energy prices. Those projections sometimes resulted in expensive above-market contracts that adversely affected native load customers. Undue reliance on projections has also resulted in uneconomic utility projects. While some reliance on forecasts is a necessity, locking in native load capacity based on imprecise forecasts (and subsequent calculations of ACT) represents a serious and unwarranted risk. Forecasting errors will occur, but native load should not have to bear the burden of these errors.

The Order does not address what will happen if a utility's forecast is too low, and this issue requires clarification. Will native load be entitled to receive sufficient capacity, even though the actual growth exceeded the forecast? Will the calculation of ATC reflect the actual

growth in native load instead of the forecasted growth? Can a utility resell capacity (not reserved for native load because of a low forecast) that is ultimately needed for native load? Is there a fallback mechanism to protect native load customers from a utility's unreasonable forecasts?

Reservation priority must protect native load and give utilities flexibility. The Order should require utilities to reserve sufficient capacity to serve the current and projected needs of native load customers, the wholesale and retail customers on whose behalf the present transmission system was built. The definition of native load customers in Section 1.19 of the tariff should explicitly include existing distribution cooperatives and others who currently provide serve to end users (e.g. · municipally-owned utilities). FERC should establish the following reservation priority: native load customers, **[9]** followed by firm contract customers, and last, non-firm customers. FERC should emphasize that the calculation of ATC must not include any capacity that may be needed by native load customers.

MOTION FOR REHEARING OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

[pp.1-22]

[1]

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

Promoting Wholesale Competition	)
Through Open Access	)
Non-discriminatory Transmission	)
Services by Public Utilities	)
	)
Recovery of Stranded Costs by	)
Public Utilities and	)
Transmitting Utilities	)
	)

MOTION FOR REHEARING OF THE PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK

PRELIMINARY STATEMENT

The recent issuance by the Federal Energy Regulatory Commission ("FERC" or "Commission") of Order Nos. 888 and 889 lays the foundation for a new era of competition in the electric industry by opening access to electric transmission

systems nationwide. This week, the Public Service Commission of the State of New York ("PSCNY") built on this foundation by declaring its intention to open the state's seven investor-owned electric utilities and the integrated New York Power Pool to wholesale competition in 1997 and to retail access by all classes of electric customers in 1998.[1] These actions make cooperative federalism a reality by bringing the benefits of competition to electric ratepayers in New York State and across the nation. Competition in the generation and energy service **[2]** businesses will lower rates and increase choice of electric providers and innovative energy services.

Accomplishing the shared goal of promoting open access and competition, however, cannot alter the Jurisdictional boundaries between FERC and the states prescribed by Congress in the Federal Power Act. Effective competition must be accomplished by observing the dual Jurisdictional framework, which prescribes that state agencies retain Jurisdiction of retail services, and encourages cooperation between the relevant state and federal administrations. Although the Commission provided deference to state authority in certain areas, FERC Order 888 intrudes on state Jurisdiction in the areas of stranded retail costs and local distribution of electricity. Accordingly, PSCNY moves

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[1]New York Pub. Serv. Comm'n Case No. 94-E-0952, In the Matter of Competitive Opportunities Regarding Electric Service, Opinion and Order Regarding Competitive Opportunities for Electric Service, Opinion No. 96-12 (issued May 20, 1996).

pursuant to Rule 713 for rehearing of FERC Order 888 as a final agency action.[1]

In Point I, PSCNY requests that FERC declare that it will not backstop state determinations on retail stranded cost recovery. Point II asks FERC to recognize that the states have authority to determine the level of retail-turned-wholesale stranded costs. Point III addresses the fact that, although Order 888 states that FERC will defer to state recommendations on distinguishing transmission from local distribution facilities, the final rules require states to apply the seven factors enunciated in the NOPR, of which PSCNY opposed five in its comments thereon. Hence, [3] PSCNY asks the commission to abandon its seven indicator test for distinguishing transmission from local distribution in favor a straightforward functional standard. Finally, although we appreciate the guidance FERC has provided for formation of independent system operators (ISOs) for power pools, the Commission's ISO principles constrain governance options. Point IV, therefore, asks FERC to clarify that it will defer to state-brokered solutions and provide maximum flexibility for creative solutions to assure open access and effective competition in "tight" (integrated) power pools.

By making this motion for rehearing, we do not seek to delay implementation of FERC's final rules. Rather, the PSCNY looks forward to working closely with FERC in implementing state and federal initiatives promoting electric competition. Accordingly, we ask the FERC to modify Order 888 to expedite implementation.

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[1] 16 U.S.C. §8251(a); 18 C.F.R. §385.713(b).

PROCEDURAL HISTORY

On June 29, 1994, the commission issued its original Notice of Proposed Rulemaking on utility stranded costs incurred during the transition to competition in the electric industry.[1] In that NOPR, the commission declared that it had Jurisdiction over rate recovery of utility investments that were stranded due to retail wheeling, and would act as a backstop to state action on retail stranded costs. The PSCNY filed initial comments on **[4]** December 8, 1994 and reply comments on January 24, 1995.[1] In those comments, we stated that "the notion of FERC generally agreeing to act as a backstop to state action, however, could impede state implementation of restructuring programs or transition policies.[2] We further noted that retail stranded costs are a state regulatory concern.

The Commission issued a notice of proposed rulemaking concerning transmission open access and a supplemental notice of proposed rulemaking on stranded cost

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[1]Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Docket No. RM-94-7-000, 59 Fed. Reg. 35274 (July 11, 1994).

[1]New York State Public Service Comments on the Proposed Rule, Docket No. RM94-7-000 (December 8, 1994); Reply Comments of the New York State Public Service Commission (January 24, 1994).

[2]NYPSC Reply Comments (January 24, 1995), at 2.

recovery on March 29, 1995.[3] Known as the "MegaNOPR", the proposed rulemaking provided, among other things, that: (1) FERC has authority over retail stranded costs and would backstop the states on utility recovery of retail stranded costs, (2) FERC would determine the level, timing and method of recovery of retail-turned-wholesale costs stranded by the creation of new wholesale entities, such as municipal electric utilities, (3) FERC had jurisdiction over transmission facilities, would determine which facilities are transmission and those that were exclusively local **[5]** distribution, and would use a seven-factor test for making that determination.

In our initial comments on the MegaNOPR, the PSCNY argued, among other points, that FERC lacks authority over retail stranded costs, including retail-turned-wholesale costs, and that the NOPR's treatment of local distribution in wholesale power transactions contravenes state authority.[1] In reply comments, we urged FERC to ameliorate the prospect of litigation over retail-turned-wholesale costs by

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[3]Promoting Wholesale Competition Through Open-Access Non-Discriminatory Transmission Service by Public Utilities, Docket No. RM95-8-000, and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Docket No. RM94-7-001, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 Fed. Reg. 17662 (April 7, 1995).

[1]Comments of the Public Service Commission of the State of New York (August 4, 1995).

allowing the states to determine the level of stranded costs to be recovered in transmission rates.[2]

On April 24, 1996, FERC issued its final rules on transmission open access and stranded cost recovery.[3] FERC Order No. S88 should generally assist the transition to a competitive electric marketplace through the filing by utilities of non-discriminatory open access transmission **[6]** tariffs, the transparent provision of information on wholesale power transactions, and the required unbundling of transmission operation functions from wholesale marketing of electricity. FERC properly noted its deference to the states on several matters, including ordering retail wheeling to ultimate customers, service reliability, generation and transmission siting, local distribution of electricity, and authority to impose

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[2]Reply Comments of the Public Service Commission of the State of New York. The PSCNY also made presentations at technical conferences convened by FERC on October 27, 1995 regarding the proposed pro forma transmission tariffs and on December 5, 1995 concerning implementation of transmission access in power pools.

[3]Previously, the Commission also issued a notice of proposed rulemaking on information systems. Real-Time Information Networks and Standards of Conduct, Docket No. RM95-9-000, Notice of Proposed Rulemaking, 60 Fed. Reg. 66182 (December 21, 1995). PSCNY filed comments on the RIN NOPR on June 29, 1995. The Commission issued a final rule on the renamed Open Access Same-Time Information System (OASIS) in FERC Order No. 889. 61 Fed. Reg. 21737 (April 24, 1996). In this motion, PSCNY does not seek rehearing of Order No. 889.

non-bypassable retail stranded cost charges. Hence, the Commission stated:

> This Final Rule will not affect or encroach upon stats authority in such traditional areas as the authority over local service issues, including reliability of local service; administration of integrated resource planning and utility buy-side and demand-side decisions, including DSM; authority over utility generation and resource portfolios; and authority to impose non-bypassable distribution or retail stranded cost charges.[1]

Unfortunately, the Commission's final rules intrude on state authority over retail stranded costs, including retail-turned wholesale costs, and state authority over the local distribution of electricity. Moreover, the final rules should be clarified to acknowledge the states' flexibility to broker solutions to transmission access in tight power pools through the implementation of an independent system operator (ISO).

[7]

POINT I
FERC SHOULD DECLARE THAT THE STATES HAVE EXCLUSIVE AUTHORITY OVER RETAIL STRANDED COSTS

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[1] Id., at 434, n 544.

A. Congress Has Assigned the States Exclusive Jurisdiction Over Retail Stranded Costs

FERC declares in Order 888 that it has jurisdiction over retail stranded costs. The order states:

> We believe that both the Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[1]

The Order further states, however, that FERC will allow utilities to seek federal recovery of stranded costs caused by state-ordered retail wheeling only in limited circumstances. Hence, the Order states that the Commission will address retail stranded cost recovery only when the state regulatory authority does not have authority to address retail stranded costs.[2]

FERC's claim of authority over retail stranded costs contradicts the language of the Federal Power Act. Section 201(a) of the Federal Power Act provides that federal regulation extends to all sales of electric energy in interstate

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[1]Order 888, at 553.

[2]Id., at 8, 553.

commerce at wholesale except those **[8]** specifically exempted, and would exclude all retail sales. Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, 211 (1964), reh'g denied, 377 U.S. 913 (1964) (emphasis added). The Supreme court has read Section 201 as drawing "a bright line easily ascertained, between federal and state jurisdiction . . ." 376 U.S. at 215. The Commission's attempt to use its power over wholesale sales to regulate the rate treatment of stranded retail[1] costs violates Congress' assignment of retail regulation to the states. Federal Power Comm'n v. Southern California Edison, 376 U.S. 205 (1964), reh'g denied, 377 U.S. 913 (1964); Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1977), reh'g denied, 405 U.S. 948 (1972); Arkansas **[9]** Electric Cooperative v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 378-80 (1983).[1]

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[1]If a state utility loses $100 in revenues because a retail customer leaves the company, the fixed costs underlying the $100 remain part of the retail (state) revenue requirement, irrespective of whether the reduced usage resulted from international developments, FERC action, or purely local conditions. That is, the fact that FERC's exercise of its power over wholesale service may have led to the stranding of costs used to serve retail customers would not, in law or logic, move those costs and the revenues supporting them into FERC's jurisdiction. Similarly, if action by state agencies affects wholesale transactions, such effects cannot alter the Jurisdictional boundaries established by Congress.

[1]The Supreme Court has reiterated that the Federal Power Act was intended to leave the states' power over retail sales undisturbed, particularly insofar as it reflected the constitutional division between federal and state power existing when the Federal Power Act was passed. That division was applied to electric utilities

Inasmuch as FERC does not have jurisdiction to determine the rate treatment of costs devoted to retail service, it lacks authority to allow recovery if a state decides not to do so. As the Supreme Court noted in Connecticut Light & Power Co. v. Federal Power Comm'n, 324 U.S. 515 (1945), "the 'insulated chambers of the states' are still laboratories where many lessons in regulation may be learned by trial and error on a small scale without involving a whole national industry in every experiment." 324 U.S. at 530.

FERC's promise to invoke its claimed jurisdiction over retail stranded costs only where states lack authority to addressed stranded costs offers little solace. These statements do not eliminate the possibility that a utility which is unhappy with a state decision on stranded costs might turn to FERC to preempt the states on stranded costs using lack of authority as its pretext.

[10]

On the other hand, if FERC simply intends to provide a forum for retail stranded cost recovery where none exists at

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in Public Utilities Comm'n of Rhode Island v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927), in which the Supreme Court held that a state regulatory commission could not regulate a wholesale transaction in interstate commerce. Congress filled the resulting gap by establishing federal regulation over wholesale transactions of electric utilities engaged in interstate commerce, but leaving retail intrastate transactions to the states. See Arkansas Electric Cooperative Corp. v. Arkansas Public Serv. Comm'n, 461 U.S. at 378-79 (1983).

the state level,[1] the PSCNY assumes that FERC will leave undisturbed state decisions on retail rate recovery. Consequently, PSCNY respectfully requests FERC to clarify its final rules to declare that it has no intention to review states' decisions on retail stranded investment.

POINT II

FERC SHOULD RECOGNIZE THAT STATES HAVE AUTHORITY TO DETERMINE THE LEVEL OF RETAIL-TURNED-WHOLESALE STRANDED COSTS

A. Congress has Assigned the States Exclusive Jurisdiction over Retail-Turned-Wholesale Stranded Costs

Order 888 asserts that FERC has jurisdiction to determine the rate treatment of costs stranded by the departure of retail-turned-wholesale customers. Moreover, over the dissent of Commissioners' Massey and Hoecker, the Order states that FERC should be the primary forum for addressing the recovery of these utility costs. While federal and state agencies often take actions that affect costs and revenues in each other's jurisdiction, such consequences cannot alter jurisdictional boundaries. Louisiana v. Federal Communications Comm'n, 476 U.S. 355 (1986). In Louisiana v. Federal Communications Comm'n, the **[11]** Supreme Court held that, although the states' setting of depreciation charges

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[1]It is difficult to envision a circumstance in which a state utility regulatory body has authority to order retail wheeling but lacks jurisdiction to address the rate consequences of its decision.

was alleged to frustrate a federal plan to modernize the telephone network, the Federal Communications Commission's alleged need to rectify the situation did not allow it to infringe on the states' jurisdiction.[1] Again, the Commission's attempt to use its power over transmission or wholesale sales to regulate the rate treatment of stranded retail costs (irrespective of whether the costs at issue were incurred to serve retail customers that became wholesale customers) violates Congress' assignment of retail regulation to the states. Federal Power Comm'n v. Southern California Edison, 376 U.S. 205 (1964), reh'g denied, 377 U.S. 913 (1964); Federal Power Comm'n v. Florida Power & Light Co., 404 U.S. 453 (1977), reh'g denied, 405 U.S. 948 (1972); Arkansas Electric Cooperative v. Arkansas Public Serv. Comm'n, 461 U.S. 375, 378-80 (1983).

B. FERC Should Modify Order 888 to Leave to the States the Issue of the Level of Stranded Costs to Be Recovered in Transmission Rates

In its Reply Comments on the NOPR, PSCNY offered a cooperative solution to the recovery of retail-turned-wholesale stranded costs. We proposed a process whereby the **[12]** states would set the level of retail-turned-wholesale stranded costs to be recovered in wholesale transmission rates set by FERC. This cooperative method, which was also

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[1]Specifically, in rejecting the FCC's claim that state regulation was affecting a federal program, and therefore could be preempted, the Court stressed that allowing the FCC to determine the pace of intrastate depreciation recovery "would be to grant to the agency power to override Congress." (476 U.S. at 374-375).

suggested by a number of state commissions,[1] would respect state interests in controlling the rate impact of stranded costs, while allowing FERC to design the method of cost recovery. Such a mechanism would also address the needs of industrial customers and other stakeholders by providing a forum before state regulators who will be more aware of their particular needs. Accordingly, PSCNY respectfully asks the Commission to modify Order 888 to recognize the states' jurisdiction to determine the level of retail-turned-wholesale costs.

C. FERC's "Reasonable Expectation" Standard Ignores a Series of Criteria Relevant to Retail Stranded Costs

Order 888 states that a utility seeking to recover stranded retail-turned-wholesale costs must show that when it incurred those costs, it had a "reasonable expectation" that the customers would continue to receive bundled retail service.[2] The Commission further states that it will apply the "reasonable expectation standard" to retail stranded cost recovery.[3] Such a test would ignore prudence, customer impact, financial viability and a series **[13]** of criteria traditionally analyzed by regulatory agencies in determining rate treatment of costs incurred with the intention of providing service. See Permian Basis Area Rate Cases, 390 U.S. 747 (1968), reh'g denied sub nom. Bass v. Federal Power

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[1]Order No. 888, at 534.

[2]Id., at 572.

[3]Id., at 570-71.

Comm'n, 392 U.S. 917 (1968); Market Street Railway Co. v. Railroad Comm'n of California, 324 U.S. 548 (1945); Jersey Central Power and Lioht Co. v. Federal Energy Regulatory Comm'n, 810 F.2d 1168 (D.C. Cir. 1987). The PSCNY applies these criteria to arrive at a just and reasonable balancing of consumer and investor interests. N.Y. Pub. Serv. Law S65; Matter of Abrams v. Public Serv. Comm'n, 67 N.Y.2d 205, 215 (1986).

The states are in the best position to determine the nature and level of stranded retail costs. Moreover, decisions by state regulatory agencies on recovery of retail stranded costs will be subject to judicial review under well-established standards in state courts. FERC should let the states decide the rate treatment of retail-turned-wholesale stranded costs.[1]

[14]

POINT III

LOCAL DISTRIBUTION SHOULD BE DISTINGUISHED FROM TRANSMISSION UNDER A FUNCTIONAL STANDARD

FERC's final transmission open access rules are responsive to PSCNY'S comments that the Commission

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[1]FERC's proposal that stranded costs be administratively determined by a one-time calculation of lost revenues is, in any event, incorrect. If volumes change over, the revenues lost by the migration of a single customer will change, yet the "stranded cost" calculation will not be adjusted.

should respect state authority over local distribution.[1] Order 888 states that the Commission will not encroach upon traditional state authority to regulate the local distribution of electricity.[2] The Commission further states that it will defer to state recommendations in distinguishing local distribution facilities from equipment used for transmission in interstate commerce when states implement retail wheeling of electricity.[3] FERC pronounced that states are free to consider indicators that respect the traditional designation of facilities as transmission versus local distribution.[4] Finally, FERC says that it will respect state authority over the service of delivering electricity to end users, even if that service entails usage of transmission facilities.[5]

PSCNY appreciates FERC'e deference to state authority over local distribution of electricity. Indeed, in our state electric competition proceeding, we have ordered the seven utility members of the New York Power Pool **[15]** to provide information and filings that will assist PSCNY in distinguishing transmission and local distribution facilities in

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[1]Order 888, at 407.

[2]Id. at 427, 429.

[3]Id. at 429.

[4]Id. at 438.

[5]Id. at 433.

the integrated New York State pool.[1] Nevertheless, we disagree with the Commission's position on two related issues: 1) the Commission's deference should extend to all state commission recommendations regarding the definition of local distribution facilities; and, 2) five of the seven assumptions are inaccurate when applied to large metropolitan areas and to remote rural areas, and should be reexamined.[2]

A. FERC Should Defer in All Instances to the States in Distinguishing Local Distribution from Transmission

Regarding Commission deference to state determinations of what facilities should be considered local distribution, the Commission should not limit its deference to instances in which states order retail wheeling. The question where interstate transmission ends and local distribution begins is arising with increasing frequency. For example, in a pending petition by Suffolk County Electric Agency (SCEA) for transmission service under section 211 of the Federal Power Act, SCEA argues that transmission facilities extend to its customers' meters and, therefore, that there are no state-

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[1]N.Y.P.S.C. Opinion No. 96-12, supra, at 35, 73 (May 20, 1996).

[2]Comments of the Public Service Commission of the State of New York, August 4, 1995, at 9.

jurisdictional local **[16]** distribution facilities involved.[1] PSCNY opposed SCEA's argument and recommended that FERC defer to our expertise in analyzing local conditions to distinguish distribution facilities from interstate transmission equipment to which a section 211 wheeling order would apply.[2] FERC should modify Order 888 to state that it will defer to state expertise in distinguishing transmission from local distribution facilities.

B. State Agencies and FERC Should Agree on a Definition that Preserves the Traditional Classification of Local Distribution Facilities

1. The Rule's Assumptions Regarding Distribution Facilities Are, In Several Respects, Erroneous

In distinguishing transmission from distribution, Order 888 states that:

> 1. Local distribution facilities are normally in close proximity to retail customers;

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[1]Suffolk County Electric Agency, Docket No. TX 96-4-000, Application for Order Requiring Transmission Service (January 17, 1996), at 19.

[2]Suffolk County Electric Agency, Docket No. TX 96-4-000, Notice of Intervention by the Public Service Commission of the State of New York (February 21, 1996), at 3-6.

2. Local distribution facilities are primarily radial in character;

3. Power flows into local distribution systems; it rarely, if ever, flows out;

4. When power enters a local distribution system, it is not **[17]** reconsigned or transported on to some other market;

5. Power entering a local distribution system is consumed in a comparatively restricted geographical area;

6. Meters are based at the transmission/local distribution interface to measure flows into the local distribution system;

7. Local distribution systems will be of reduced voltage.[1]

With the exceptions of indicators 3 and 5, these assumptions are not accurate when applied to large metropolitan areas and to remote rural areas.

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[1]Order 888, at 402.

Concerning the first indicator, local distribution facilities are not necessarily close to retail customers. For example, local distribution lines cover great distances in the New York metropolitan area before voltages are stepped down to consumption levels.

With respect to the second indicator, the rules' assumption that local distribution facilities are primarily radial in character fails to account for network systems. The distribution system for large portions of many metropolitan areas (e.g., New York City, San Francisco) consists of a large grid of loops, referred to as a network system.

Regarding the fourth indicator, reconsignment or transportation of power to different markets can and does occur at the local distribution level. Again, the market **[18]** features of power transactions have little to do with the technical characteristics of local distribution grids.

With respect to the sixth indicator, meters are frequently not part of the transmission/distribution interface, and may also be present at other points in interstate transmission or local distribution systems. The presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins.

Concerning the seventh indicator, local distribution systems are not necessarily of reduced voltage. The NOPR had stated that, based on FERC Form No. I filings, transmission facilities appeared to operate at greater than 30

kV and distribution is usually less than 40 kV.[1] That is often not the case in New York State. In rural areas of upstate New York, some lines operating at 23 kV are regarded as transmission lines. By contrast, the New York city metropolitan area operates lines at 69 kV as local distribution facilities. Order 888 did not correct this error.

2. The State/FERC Definition of Distribution Facilities Should Focus on the Functional Characteristics of Local Electric Systems

Only two of the seven technical assumptions adopted by FERC correctly define local distribution. **[19]** Specifically, interstate transmission ends and local distribution begins where: (1) electricity flows into a comparatively restricted geographic area and does not flow back out of that area, and (2) the power is consumed in that area. The Commission should simplify its seven-factor test to this functional measure of local distribution, coupled with the traditional classification of the facilities by the state regulatory body or, in the alternative, what the utility has traditionally classified as distribution. This distinction would be more workable and accurate. Accordingly, FERC should modify Order 888 to adopt the functional standard proposed by PSCNY for distinguishing transmission from local distribution.

[1]Open Access NOPR at 285 n. 396.

POINT IV

FERC SHOULD PROVIDE FLEXIBILITY IN THE FORMATION OF INDEPENDENT SYSTEM OPERATORS

Order 888 encourages the formation of independent system operators (ISOs) to assure comparable transmission access in integrated power pools, such as the New York Power Pool. The Commission sets forth eleven principles to guide the formation of ISOs.[1] PSCNY shares FERC's vision that an ISO is the appropriate structure for assuring comparable transmission access where tight power pools exist. An ISO will also ensure safe and reliable service and the infrastructure for effective retail competition in New York. Accordingly, in its order on restructuring the electric industry, PSCNY stated that it expects the seven electric **[20]** and combination utilities and the New York Power Authority to complete a proposal for establishing an ISO for New York by October 1, 1996.[1]

The ISO principles do not provide adequate flexibility for establishing an ISO that will meet New York's needs. For example, in its first principle, FERC states that "The ISO's governance should be structured in a fair and non-discriminatory manner".[2] In interpreting this principle, the

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[1]Order 888, at 279-86.

[1]N.Y.P.S.C. Opinion No. 96-12, supra, at 35, 73 (May 20, 1996).

[2]Order No. 888, at 280.

commission states that an ISO should be independent of market participants, including control by transmission owners.[3] Accordingly, FERC would apparently reject an ISO proposal that provided for governance by transmission owners.

The parties to New York's electric competition proceeding[4] are discussing formation of an ISO with the following features:

1. Market pricing rules are established by a multi-party board that is not under the control of any one class of market participant;

[21]

2. The establishment and implementation of reliability rules and market rules is handled by a system operator controlled by transmission owners that have divested competitive generation; and,

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[3] Id.

[4] N.Y.P.S.C. Case 94-E-0951, In the Matter of Competitive Opportunities Regarding Electric Service. The parties to the New York State proceeding have been discussing formation of an ISO for the integrated New York Power Pool for several months. PSCNY has not received or approved any ISO proposal to date.

3. Transmission owners would recover full embedded costs independent of generation dispatch or transmission system operation, so that transmission owners would have no vested interest in decisions on access to, or operation of, the transmission system.

Even though under this proposed model the transmission owners control the system operator, it appears to be consistent with FERC's first ISO principle of fair and non-discriminatory governance because the transmission owners would own no competitive generation. Although the NYPSC has made no decisions on ISO governance, it would not like to see this or other options foreclosed. Consequently, to ensure the formation of an ISO that meets the shared objectives of FERC and PSCNY, the Commission should clarify Order 888 to state that it will allow flexibility to states and utilities in structuring proposals that meet the goals underlying the ISO principles.

CONCLUSION

For the reasons stated above, the Federal Energy Regulatory commission should grant the motion for rehearing of the Public Service Commission of the State of New York **[22]** and modify the final rules contained in order 888 as indicated.

Respectfully submitted,

/s/_____

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DATED: May 24, 1996
Albany, New York

REQUEST OF THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS FOR REHEARING

[p. 1]

BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION
Washington, D.C.

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

Promoting Wholesale Competition	)
Through Open Access	)
Non-discriminatory Transmission	)
Services by Public Utilities	)
	)
Recovery of Stranded Costs	)
By Public Utilities and	)
Transmitting Utilities	)
	)

REQUEST OF THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS FOR REHEARING

Pursuant to Rule 713 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.713, the National Association of Regulatory Utility Commissioners (NARUC) hereby requests rehearing of Order No. 888 issued by the Federal Energy Regulatory Commission (FERC or the

Commission) in the above-captioned proceeding on April 24, 1996. 60 Fed. Reg. 21540 et seq. (May 10, 1996).

CONCISE STATEMENT OF ALLEGED ERROR

The NARUC respectfully submits that Order No. 888 contains the following errors that should be corrected upon rehearing:

- The Commission's assertion of exclusive jurisdiction over transmission services provided retail consumers on an unbundled basis is inconsistent with the Federal Power Act's allocation of jurisdictional authority between the Commission and the States;

- The Commission's assertion of "primary" authority to provide for the recovery of retail costs of service that are "stranded" when a group of end-users convert to wholesale customers under procedures established in State law exceeds the Commission's authority under the Federal Power Act;

* * * * *

[4]

B. The Commission Should Reverse its Assertion of Jurisdiction over the Rates, Terms and Conditions of Unbundled Retail Transmission Services

In Order No. 888, the Commission restates its conclusion that "it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities." Slip op. at 400. We respectfully submit that this conclusion is erroneous, and urge its reversal on rehearing for the following reasons.

First, as the Commission notes, the allocation of jurisdiction between the Commission and the States enacted by Congress in both the Federal Power and Natural Gas Acts

> grew out of a market structure in which electricity and transmission generally were bought and sold on a bundled basis. As a result, most transactions included either a retail or wholesale sale of electric energy and jurisdictional lines were drawn on the basis of this sale. Thus, the cases [construing these statutes] simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry.
>
> Id. at 428 (emphasis added)

Moreover, ambiguous case law is not the only problem in analyzing this jurisdictional question. As the Commission stated in March 1995 in the Notice of Proposed Rulemaking (NOPR) in this docket, the legislative history of the Federal Power Act "does not provide any definitive answers" as well. NOPR at 258.[2]

As NARUC stated in its October 4, 1995 reply comments (at 5-7), we agree with the Commission that the FPA's allocation of jurisdictional responsibility was designed in a far different regulatory era to address a very specific problem: filling the so-called Attleboro gap **[5]** in which States were found incapable of regulating interstate wholesale power sales transactions.[3] We further agree that the case law of that era is not dispositive concerning the question of unbundled retail transmission services either because the cases do not involve the transmission of power to retail customers[4]

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[2]While including some analysis in the preamble to Order 888, the FERC included as Appendix G to Order No. 888 the bulk of its legal analysis of its exclusive authority over the rates, terms and conditions of unbundled retail transmission. While the Commission believes that the statute is clear on its face as to this issue, it attempts to buttress its analysis by relying on this ambiguous legislative history and out-dated case law.

[3]Public Utilities Commission v. Attleboro Steam & E. Co., 273 U.S. 83 (1927).

[4]Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943); FPC v. Southern California Edison Co., 376 U.S. 205 (1964) (the Colton case); Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission, 461 U.S. 375 (1983).

or fence off local distribution from Federal regulation.[5] As the Commission acknowledged in the NOPR (at 266-8), at least one Court of Appeals, relying on Congress' intent to close the Attleboro gap concerning wholesale power sales, explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services, lending support to NARUC's claim that the Commission should apply the same analysis -- wholesale versus retail -- to the question of unbundled retail transmission.[6]

Second, we agree that the legislative history is not helpful in resolving this jurisdictional question, and provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a State commission to the FERC. If anything, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services as the Commission concludes. Indeed, as recently as 1992 when it enacted the Energy Policy Act (EPAct), Congress reaffirmed the wholesale/retail distinction when it amended section 212 of the FPA to prohibit the **[6]** Commission from issuing orders that require transmission of electric energy to a retail consumer, or that are or would be otherwise inconsistent with State-regulated retail marketing areas of electric utilities. §§212(g) and (h). Moreover, in EPAct, Congress included a specific provision protecting State authority "concerning the

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[5]Connecticut Light & Power Co. v. FPC, 334 U.S. *515* (1945); Duke Power Co. v. FPC, 401 F.2d 930 (D.C. Cir. 1968).

[6]Wisconsin-Michigan Power Co. v. FPC, 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953).

transmission of electric energy directly to an ultimate consumer" from interference by the Commission's newly-expanded authority to order wholesale transmission services. §212(h).

Third, the seven-factor test that the Commission adopts in Order No. 888 (at 435-6) to apply to the transmission/distribution analysis creates the further difficulty that it does not result in the "bright line" of the sort that the Supreme Court discussed in the Colton case where the wholesale versus retail dichotomy was perhaps most definitively expressed. Rather, the Commission's test necessarily involves a facility-by-facility categorization of utility systems on a company-specific basis, a process hardly consistent with the Court's decision to "mak[e] unnecessary such case-by-case analysis." 376 U.S. at 214.

Accordingly, the NARUC again urges the Commission to adopt on rehearing a test that results in no change in the allocation of jurisdiction between FERC and the States in the retail wheeling/customer choice case from the situation in which electric energy is provided an end user by the utility supplying the delivery service. The Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer is subject to the jurisdiction of the State commission regulating the utility, regardless of the identity of the party generating or reselling the power or the facilities used to transport the power.

[7]

There would be a number of important benefits if this proposal were adopted. First, the Commission would be

implementing a bright line test: delivery of electric energy to an end user would be State-jurisdictional regardless of who generates or supplies the power.[7] As a result, the Court's admonition in Colton against case-by-case analysis as required by Order No. 888 would be heeded. Importantly, a jurisdictional test which focusses on the retail status of the customer receiving the delivery service is entirely consistent with Colton's analysis of wholesale and retail power sales. To the extent that Colton demands a bright-line test as a matter of law, this proposal is one of the few workable and easily understood alternatives, given that under no conceivable analysis can the Commission conclude that the delivery of third-party power to an end user is exclusively FERC-jurisdictional, i.e., never involves a State-jurisdictional distribution component.

Finally, we submit that a decision which definitively clarifies jurisdiction over delivery of third-party power to an end user in the manner we have suggested will actually

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[7]In, Order No. 888, the Commission appears to conclude that a State-established program allowing for retail customers to choose their source of generation necessarily results in the creation of an unbundled transmission service, and hence effects a shift in jurisdiction from the State commission to the FERC. Slip op. at 430-1. The commission does not address the point we raised in our reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. Id. Without any real explanation, the Commission simply assumes -- erroneously in our view -- that a "resulting transmission transaction" is created when power sale is sold to a retail consumer by someone other than the utility delivering the power.

promote the Commission's competitive goals. While Order No. 888 does provide certain assurances that the Commission will be sensitive to State initiatives, it remains a distinct possibility that States which might consider implementing pro-competitive customer choice programs will be hesitant **[8]** to do so due to their concern that their commissions will be precluded from regulating much (or any) of the retail delivery service provided by the utility.

In sum, the NARUC submits that for sound legal and practical reasons, the Commission should conclude that when a State determines to enable a retail consumer to purchase power from a third-party provider, its State commission retains the authority to regulate the rates, terms and other conditions of the delivery service provided by the utility to that consumer.

C. The Recovery of Retail Stranded Costs, in Either the Retail-turned-Wholesale or Retail Wheeling Case is Subject to the Exclusive Jurisdiction of the States

The NARUC once again respectfully requests that on rehearing, the Commission withdraw that portion of Order No. 888 which provides utilities the opportunity to apply to FERC to recover so-called "retail stranded costs." The Commission lacks the legal authority either to take "primary jurisdiction" in the retail-turned-wholesale case, or to act as a backstop in the retail wheeling case when a State lacks authority to address the issue. Accordingly, FERC must leave the identification, measurement, allocation and recovery of the costs incurred by a utility to serve its retail customers for the State legislatures and commissions to resolve.

Under section 201(a) of the FPA, FERC's jurisdiction is limited to 'the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce," and further, extends "only to those matters which are not subject to regulation by the States." Further, section 201(b) of the statute expressly excludes from the Commission's authority "facilities used for the generation of electric energy" as well as distribution facilities. Costs incurred by a utility to serve its retail customers, whether they be the costs of utility-owned generation facilities, demand-side management programs, "QF" contracts, or so-called **[9]** "regulatory assets," do not involve the sale of electric energy at wholesale nor interstate transmission services, and are therefore not apprehended by the Commission's wholesale sales and transmission jurisdiction. And since both of the scenarios in which FERC is prepared to act to authorize cost recovery (i.e., "municipalization" and retail wheeling) cannot occur without reliance upon the operation of State laws and regulations, it simply cannot be the case that the recovery of retail costs by a utility is "not subject to regulation by the States."

We have not ignored the fact that FERC's jurisdiction under section 201 has been given an expansive construction in judicial opinions issued since the FPA was enacted 60 years ago, nor do we doubt that "electrons do not respect State boundaries." However, even the broadest reading of section 201 cannot provide FERC jurisdiction over unamortized <u>generation</u> (or other) costs held in retail rate base (or otherwise subject to recovery in retail rates) for no other reason than an arguably jurisdictional <u>transmission</u> service provides the Commission a "toll booth" for the recovery of costs that would otherwise be beyond its grasp.

The lack of Commission authority under the FPA to address retail costs applies across the board; however, there are some differences between the two cases (municipalization and retail wheeling) to which we now turn.

APPLICATION OF THE COALITION FOR A COMPETITIVE ELECTRIC MARKET FOR RECONSIDERATION AND CLARIFICATION OR, IN THE ALTERNATIVE, REHEARING

[p. 1]

UNITED STATES OF AMERICA
Before The
FEDERAL ENERGY REGULATORY COMMISSION

[Filed May 24, 1996]

Docket Nos. RM95-8-001 and RM94-7-002

NOTICE OF PROPOSED	)
RULEMAKING	)
REGARDING PROMOTING	)
WHOLESALE COMPETITION	)
THROUGH OPEN ACCESS	)
NON-DISCRIMINATORY	)
TRANSMISSION SERVICES BY	)
PUBLIC UTILITIES	)
	)
SUPPLEMENTAL NOTICE OF	)
PROPOSED RULEMAKING	)
REGARDING RECOVERY	)
OF STRANDED COSTS BY	)
PUBLIC UTILITIES AND	)
TRANSMITTING UTILITIES	)
	)

APPLICATION OF THE COALITION FOR A COMPETITIVE ELECTRIC MARKET FOR RECONSIDERATION AND CLARIFICATION OR, IN THE ALTERNATIVE, REHEARING

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May 24, 1996

* * * * *

[pp. 4-8]

[4]

REQUEST FOR REHEARING

I. DEPARTURES FROM SERVICE COMPARABILITY

A. All Transmission Must Be Unbundled

1. Transmission to retail customers -- The Commission wisely questioned in the underlying notice of proposed rulemaking whether undue discrimination can be eradicated in a "bifurcated" market in which transmission for wholesale is unbundled and transmission for retail is not:

> This will result in service under two separate arrangements -- an explicit wholesale transmission tariff filed at the Commission and an *implicit* retail transmission tariff governed by a state regulatory body. It also raises the possibility that the quality of transmission service for retail purposes will be superior to the quality of transmission service offered for wholesale purposes.

Notice of Proposed Rulemaking Regarding Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities, 60 Fed. Reg. 17,662 at 17,681 (1995) (emphasis added) [hereinafter, "NOPE"]. Despite the Commission's recognition of this risk of service inequality, and its further recognition in the Rule that unbundling transmission from retail service "would be helpful in achieving comparability," Order, 61 Fed. Reg. at 21,577, it fails to require that all transmission service be unbundled from retail services. This failure is arbitrary and irreconcilable with the Commission's concurrent determination in connection with the rules pertaining to stranded-cost recovery that it has jurisdiction over the rates, terms and conditions of **[5]** unbundled interstate transmission services by public utilities to retail customers, and that it has the authority to address retail stranded costs through its jurisdiction over such services. Order. 61 Fed. Reg. at 21,650. Commission jurisdiction over *all* transmission has a solid legal foundation. Because of the manner in which electric power flows, the Supreme Court repeatedly has affirmed that virtually all transmission is in interstate

commerce.[2] Granted, the Commission heretofore has not exercised its Federal Power Act ("FPA") authority to regulate transmission to a retail customer. This does not negate the existence of the Commission's authority.

Perpetuation of a discriminatory dual market, absent *complete* unbundling, finds a clear parallel in the Commission's experience from restructuring the natural gas industry. Following introduction of open-access transportation via Order No. 436, service comparability continued to elude gas markets:

> [T]he firm transportation embedded within the *pipelines' bundled, city-gate, firm sales service is superior* to the pipeline's open-access firm transportation service. This means that pipelines and other gas suppliers are not competing on an even basis for sales customers, even where firm transportation is available to move the gas sold by the pipelines' competitors.

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[2] *E.g., FPC v. Florida Power & Light Co.*, 404 U.S. 453, 463 (interstate power "commingles in a bus"), *reh'g denied*, 405 U.S. 948 (1972); *FPC v. Southern California Edison Co.*, 376 U.S. 205, 215-16, *reh'g denied*, 377 U.S. 913 (1964); *Connecticut Light & Power Co. v. FPC*, 324 U.S. 515, 533, 536 (1945); *see also Florida Power & Light Co.*; 29 F.E.R.C. ¶61,140 at 61, 291(1984) ("transportation of power [on] grid . . . used in interstate commerce is subject to this Commission's jurisdiction, even when all the parties to the wheeling transaction are located within the same State").

[6]

Pipeline Service Obligations and Revisions to Regulations Governing Self-Implementing Transportation; and Regulation of Natural Gas Pipelines after Wellhead Decontrol, Order No. 636, 57 Fed. Reg. 13,267 (1992), [Regs. Preambles] III F.E.R.C. Stats. & Regs. ¶30,939 at 30,402 (1992) (emphasis added) [hereinafter "Order No. 636"]. Ultimately, in order to achieve "an even basis for competition," the Commission in Order No. 636 was compelled to unbundle transportation completely, not only from the pipeline's citygate wholesales, but also from the pipeline's direct retail sales. *See* 18 C.F.R. §284:10 (1994) (requiring pipelines to phase in conversion rights for all firm sales service customers whose contracts preceded Order No. 436).

Just as open access *alone* did not uproot inequality between unbundled transportation provided to third-party shippers and the bundled transportation that the pipelines provided to themselves to make citygate sales, the *pro forma* tariffs *alone* cannot establish comparability between the transmission service that a public utility provides to its retail sales functions and the wholesale transmission services that it provides to others. Ineluctably, discrimination will persist until there is total unbundling and consumers *of all* transmission services, wholesale and retail, take service pursuant to the same tariff at posted rates. The Commission's authority *and responsibility* under the FPA to address such discriminatory differences between wholesale and retail markets is well established in the prevailing decisional precedents. *See FPC v. Conway Corp.*, 426 U.S. 271, 273 (1976).

[7]

The failure to unbundle transmission to retail customers is also squarely at odds with the Commission's decisional precedents under the Natural Gas Act CNGA"). In *Mississippi River Transmission Corp. v. FERC,* 969 F.2d 1215 (D.C. Cir. 1992), the court affirmed the Commission's interpretation of NGA section 1 (b), 15 U.S.C. §717(b) (I 988), as authorizing the Commission to regulate the price of transportation service that MET provided in support of certain firm direct sales. In relevant part, NGA section 1 (b) is identical to FPA section 201(b): "The provision of this chapter shall apply to the transportation of natural gas in interstate commerce . . . ." Based on this broad grant of jurisdiction, the court held that:

> FERC is not barred from regulating a pipeline's interstate transportation of natural gas merely because the sale of the gas being transported is not itself subject to federal regulation. FERC's authority over such transactions is beyond dispute.

969 F.2d at I217 (citing *FPC v. East Ohio Gas Co.,* 338 U.S. 464, 468 (1950)); *accord Alabama Tennessee Natural Gas Co.,* 64 F.E.R.C. ¶61,084 at 61,846 (1993); *Carnegie Natural Gas Co.,* 63 F.E.R.C. ¶61,103 at 61,612 (1993). In reaching this conclusion, the court rejected MET's contention that the Commission's NGA §1(b) jurisdiction to regulate the price, terms and conditions of interstate transportation is divested whenever the subject transportation is bundled with

a non-jurisdictional sale.[3] The court found this contention untenable because it would invite manipulation:

[8]

> As far as the statute is concerned, there would be no doubt of FERC's section l(b) authority if MRT, instead of charging a bundled price, had charged separately for the gas itself. To accept MRT's position would therefore be tantamount to conferring on private parties the power to decide whether FERC could set the rate for interstate transportation. Private parties would have this power because it would be entirely up to them whether to structure a direct sale and interstate transportation transaction in terms of a bundled price or separate charges.

Id. at 1218. Just as the Commission's NGA section l(b) jurisdiction to regulate natural gas transportation to retail customers was "beyond dispute" in *Mississippi River,* it is equally beyond dispute that the Commission possesses FPA section 201(b)jurisdiction to unbundle and regulate electricity transmission in interstate commerce to a retail customer.

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[3]The NGA and the FPA are different with respect to the certificate of public convenience and necessity (" PC&N") that a natural gas company must obtain under NGA §7, 15 U.S.C. §717f(c) (1988), in advance of providing any jurisdictional service. There is no analog to the PC&N process in the FPA. The Commission's §7 jurisdiction over transportation was not contested in *Mississippi River*. *See* 969 F2d at 1217. Rather, only the Commission's authority under §1(b) to regulate the price of gas pipeline transportation to retail customers was at issue.

In sum, there is no rational basis for regulating factually undifferentiated uses of the transmission lines differently. Achieving and policing comparability will require the Commission to go beyond artificial distinctions between wholesale and retail transactions and insist that all transmission providers and customers confront the same unbundled market.

FEDERAL ENERGY REGULATORY COMMISSION
ORDER 888-A

[Issued March 4, 1997]

Docket Nos. RM95-8-0001and RM94-7-002

Order No. 888-A

* * * * *

[pp. 30,172 - 30,182]

[30,172]
62 F.R. 12274 (March 14, 1997)

18 C.F.R. Part 35

Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities

AGENCY: Federal Energy Regulatory Commission.

ACTION: Final rules; order on rehearing.

SUMMARY: The Federal Energy Regulatory Commission (Commission) reaffirms its basic determinations in Order No. 888 and clarifies certain terms. Order No. 888 requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. Order No. 888 also permits public utilities and

transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: Changes to Order No. 888 made in this order on rehearing will become effective on [insert date 60 days after date of publication in the *Federal Register*].

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contractor, La Dorn Systems Corporation. La Dorn Systems Corporation is also located in the Public Reference Room at 888 First Street, N.E., Washington, D.C. 20426.

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I. Introduction and Summary

On April 24, 1996, the Commission issued Final Rules (Order Nos. 888 and 889) intended to remedy undue discrimination in the provision of interstate transmission services by public utilities and to address the stranded costs that may result from the transition to more competitive electricity markets.[1] At the heart of these rules is a requirement that prohibits owners and operators of monopoly transmission facilities from denying transmission access, or

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[1]Promoting Wholesale Competition Through Open Access Non- discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Order No. 888, 61 FR 21,540 (May 10, 1996), *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,036, *clarified*, 76 FERC ¶61,009 and 76 FERC ¶61,347 (1996). Order No. 889 [*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* ¶31,035], is an accompanying rule and specific rehearing arguments on that rule will be addressed separately.

offering only inferior access, to other power suppliers in order to favor the monopolists' own generation and increase monopoly profits -- at the expense of the nation's electricity consumers and the economy as a whole.

The electric utility industry today is not the industry of ten years ago, or even **[30,176]** five years ago. While historically it was assumed that local utilities would be the only ones to generate and transmit power for their customers, today there is a broad array of potential competitors to supply power and widespread transmission facilities that can carry power vast distances. But competitors cannot reach customers if they cannot have fair access to the transmission wires necessary to reach those customers. It is against this industry backdrop that the Commission in Order No. 888 exercised its public interest responsibilities pursuant to sections 205 and 206 of the Federal Power Act (FPA), to reexamine undue discrimination in interstate transmission services and the effect of that discrimination on the electricity customers whom we are bound to protect under the FPA.

We here reaffirm the legal and policy bases on which Order No. 888 is grounded. Utility practices that were acceptable in past years, if permitted to continue, will smother the fledgling competition in electricity markets and undermine the national policies reflected in the Energy Policy Act of 1992 to encourage the development of competitive markets. We firmly believe that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also require us to do so, as necessary to eliminate undue discrimination and protect electricity customers. The record supports our conclusion that, absent open access, undue discrimination will continue to be a fact

of life in today's and tomorrow's electric power markets. As recent events clearly demonstrate, unbundled electric transmission service will be the centerpiece of a freely traded commodity market in electricity in which wholesale customers can shop for competitively-priced power.

The only way to effectuate competitive markets and remedy discrimination is through readily available, non-discriminatory transmission access. The Commission estimates the potential quantitative benefits from such access will be approximately $3.8 to $5.4 billion per year in cost savings, in addition to the non- quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion.

Order No. 888 has two central components. The first requires all public utilities that own, operate or control interstate transmission facilities to offer network and point-to-point transmission services (and ancillary services) to all eligible buyers and sellers in wholesale bulk power markets, and to take transmission service for their own uses under the same rates, terms and conditions offered to others. In other words, it requires non-discriminatory (comparable) treatment for all eligible users of the monopolists' transmission facilities. The non-discriminatory services required by Order No. 888, known as open access services, are reflected in a pro forma open access tariff contained in the Rule. The Rule also requires functional separation of the utilities' transmission and power marketing functions (also referred to as functional unbundling) and the adoption of an electric transmission system information network.

The second central component of Order No. 888 was to address whether and how utilities will be able to recover costs that could become stranded when wholesale customers use the open access tariffs, or FPA section 211 tariffs,[2] to leave their utilities' power supply systems and shop for power elsewhere. Because of competitive changes occurring at the retail level, as numerous states have begun retail transmission access programs, Order No. 888 also clarifies whether and when the Commission may address stranded costs caused by retail wheeling and the extent of the Commission's jurisdiction over unbundled retail transmission. The Commission further addresses the circumstances under which utilities and their wholesale customers may seek to modify contracts made under the old regulatory regime, taking into account the goals of reasonably accelerating customers' ability to benefit from competitively priced power and at the same time ensuring the financial stability of electric utilities during the transition to competition.

[30,177]

137 entities filed requests for rehearing and/or clarification of Order No. 888. While these parties raise a variety of arguments -- including legal, policy, and technical arguments -- the majority (including a majority of public utilities) agree that we need to harness the benefits that competitive electricity markets can bring to the nation. The

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[2]Under section 211 of the FPA, the Commission, on a case-by- case basis upon application by an eligible customer, may order both public utilities and non-public utilities that own or operate transmission facilities used for the sale of electric energy at wholesale to provide transmission services to the applicant if it finds it is in the public interest to issue such order.

disagreements primarily focus on the mechanics of how we should do this, who should pay the costs of the transition to competition, and how long the transition should take.

First, parties disagree on what is necessary to remedy undue discrimination and to develop truly competitive wholesale markets. Many focus specifically on the tariff terms and conditions of good transmission access and seek changes in the Order No. 888 pro forma tariff. In response to these types of rehearing arguments, the Commission has fine-tuned or changed some of the pro forma tariff terms and conditions to better ensure that they do not permit discrimination and that they result in well-functioning markets. Other petitioners focus on additional structural changes which they believe are necessary, such as mandatory corporate restructuring (divestiture of generation assets) or mandatory creation of independent transmission system operators (ISOs). With regard to restructuring, the Commission continues to believe that functional unbundling of the utility's business, not corporate divestiture or mandatory ISOs, is sufficient to remedy undue discrimination at this time.

The most contentious arguments raised on rehearing involve how we deal with the transition costs associated with moving to competition. Some utilities have invested millions of dollars in facilities and purchased power contracts based on an explicit or implicit obligation to serve customers and the expectation that those customers would remain on their systems for the foreseeable future. These utilities face so-called "stranded costs" which, if not recovered from the customers that caused the costs to be incurred, could be shifted to other customers.

There are two basic categories of rehearing arguments regarding stranded cost recovery. Most utilities want a guarantee from this Commission that they will recover all stranded costs, whether caused by losing retail customers or wholesale customers. Many customers, on the other hand, want to be able to abrogate existing power supply contracts so that they can immediately leave their current suppliers' systems and shop for cheaper power elsewhere, without paying the sunk costs that their suppliers incurred on their behalf.

In response to these diverse arguments, the Commission has struck a reasonable balance that, for certain defined circumstances, permits utilities the opportunity to seek extra-contractual recovery of stranded costs from their departing customers and permits customers the opportunity to make a showing that their contracts should be shortened or terminated. Based on our experience in the natural gas area, we have learned that it is critical to address these issues early, but we also have chosen an approach different from that taken in the gas area because of the different circumstances facing the electric industry.

In balancing the wide array of interests reflected in the rehearing petitions, we have made a number of clarifications and granted rehearing on some issues, but we reaffirm the core elements and framework of Order No. 888. Since the time the final rules issued, as discussed in Section III, the pace of competitive change has continued to escalate in the industry at both the wholesale and retail levels as competitors, customers and state regulatory authorities aggressively seek ways to lower the price of electricity. We therefore believe it is all the more critical that we remedy undue discrimination

in interstate transmission services now, and that we do so generically, if we are to fulfill our responsibilities under the FPA to protect consumers and provide a fair and orderly transition to new competitive markets.

Finally, with respect to environmental issues associated with this rulemaking, certain parties on rehearing continue to challenge the adequacy of our Final Environmental Impact Statement (FEIS). The central issues are whether the Final Rule will increase emissions of nitrogen oxides (NO_x) from certain fossil-fuel fired generators, which could affect air quality in downwind areas to which these emissions may be carried, and the Commission's authority to mitigate environmental consequences.

[30,178]

We deny rehearing on the environmental issues raised and affirm our conclusion that we have satisfied our obligations under NEPA. As discussed in detail in the Final Rule, this rulemaking is expected to slightly increase or slightly decrease total future NO_x emissions, depending on whether competitive conditions in the electric industry favor the utilization of natural gas or coal as a fuel for the generation of electricity. We also examined mitigation options over the longer term, and found that the preferred approach for mitigating any adverse environmental consequences would be for the Environmental Protection Agency (EPA) and the states to address the problem through regulatory authorities available under the Clean Air Act. The petitions for rehearing have not persuaded us to change this approach. Indeed, we note that since the issuance of Order No. 888, the EPA has concluded that the Rule is unlikely to have any immediate significant adverse environmental impact and thus concurred

that the Commission's analysis is adequate under NEPA. We further note that EPA has recently taken steps under the Clean Air Act to address NOx emissions as part of a comprehensive emissions control program, along the lines endorsed by the Commission in the EIS.

In summary, the Commission believes that our authorities under the FPA not only permit us to adapt to changing economic realities in the electric industry, but also require us to do so to eliminate undue discrimination and protect electricity customers. The measures required in Order No. 888 are necessary to remedy undue discrimination in interstate transmission services and provide an orderly and fair transition to competitive bulk power markets.

To assist the reader, we provide below a section-by-section summary of key elements of this Order on Rehearing.

Scope of the Rule

In this section we discuss petitions to rehear our requirement that transmission and power sales services be contracted for separately (unbundled). We reaffirm that this requirement is a reasonable and workable means of assuring non- discriminatory open access transmission. In doing so we refuse invitations to require that utilities under our jurisdiction divest themselves of generation or transmission assets. We do, however, make an important clarification involving how we will deal with existing contracts that contain so-called Mobile-Sierra clauses (clauses under which one or both parties agreed not to seek modification of contract terms unless they could show that it is contrary to the public interest not to permit the modification).

In Order No. 888 we concluded that contracts would not be abrogated by operation of the Rule. Instead, preexisting contracts would continue to be honored until such time as they were revised or terminated. We also found that those who were operating under pre-existing requirements contracts containing *Mobile-Sierra* clauses would nonetheless be allowed to seek reform of the contracts on a case-by-case basis. On rehearing we affirm that public utilities will be allowed to file to amend their *Mobile-Sierra* contracts for the limited purpose of providing an opportunity to seek recovery of stranded costs, without having to make a public interest showing that such cost recovery should be permitted. However, these utilities will have the burden, on a case-by-case basis, of showing that they had a reasonable expectation of continuing to serve the departing customer after the contract term. We clarify that if the utilities under such contracts seek to modify provisions that do not relate to stranded costs, they will have the burden of showing that the provisions are contrary to the public interest.

We here make clear that, in turn, customers will be allowed to file to amend their *Mobile-Sierra* contracts to modify any contract term or to terminate the contract, without having to make a showing that the contract terms are contrary to the public interest. Instead, customers seeking modifications must demonstrate that the provisions they wish modified are no longer "just and reasonable." We reaffirm our conclusion in the Final Rule that if a customer seeks to shorten or eliminate the term of its contract, however, any contract modification approved by the Commission will provide for appropriate stranded cost recovery by the customer's supplying utility.

These various provisions meet the two-fold need to deal with stranded costs and the contracts under which those costs were incurred. However, as described in **[30,179]** Order No. 888, the opportunity to reform Mobile-Sierra contracts extends only to a limited set of contracts -- those entered into on or before July 11, 1994, for requirements power.

Comparability

In this section we deal with those requesting rehearing of our conclusions regarding what "comparable" service is, who is eligible for that service, and how it is to be implemented. We reaffirm our finding that, as a matter of law, we have jurisdiction over the rates, terms and conditions of unbundled transmission service provided to retail customers. We also clarify that we have authority to order "indirect" unbundled retail transmission services and that if such transmission is ordered by us in the future, or if it is provided voluntarily, otherwise eligible customers may obtain such service under the open access tariff. We expect public utilities to provide such service in the future and, if they do not, we will not hesitate to order it.

We modify in two respects the definition of who is eligible for open access transmission service. First, we clarify that, with respect to service that this Commission is prohibited from ordering by section 212(h) of the Federal Power Act (retail wheeling directly to an ultimate consumer and "sham" wholesale wheeling), entities are eligible for such service under the tariff only if it is provided pursuant to a state requirement or is provided voluntarily. Second, we clarify that retail customers taking unbundled service pursuant to a state requirement (i.e., direct retail service) are eligible for

such service only from those transmission providers that the state orders to provide service. These changes are made to make clear that our rules cannot be used to circumvent the proscriptions placed on the Commission against ordering direct retail wheeling.

Ancillary Services

In this section we deal with petitions to rehear our definitions of ancillary services -- those services such as scheduling, voltage control, and supplemental reserve service that must or can attend the providing of transmission service -- as well as the provisions involving these services. We reaffirm that tariffs must separately state the charges for these services. We do modify some of the definitions of these services to conform to industry needs and practices. Most importantly, we make clear that the transmission provider's sale of ancillary services associated with providing basic transmission service is not a wholesale merchant function and thus does not violate the standards of conduct imposed with Order No. 889.

Coordination Arrangements

The requirement to provide non-discriminatory open access transmission applies to any agreement between utilities that contains transmission rates, terms or conditions. This includes pooling arrangements and agreements between companies contracting to provide each other mutually beneficial transmission services. In Order No. 888 we laid out rules under which the open access comparability requirements would apply to tight and loose power pools, public utility holding companies and bilateral coordination agreements. We

also set out principles that would govern our approval of independent system operator (ISO) agreements.

In this section we affirm the rules governing coordination agreements. In doing so we clarify the definition of "loose pool." We also make clear that, unlike in other situations where we require utilities to provide not only the services they provide themselves but those they could provide themselves, we will require members of loose pools to offer to third parties only those transmission services that they provide themselves under their pool-wide agreements.

We also reaffirm our strong commitment to the concept of ISOs and the ISO principles described in Order No. 888. In doing so we reject arguments that we should require that ISOs be formed. At the same time, we emphasize that while there is no "cookie-cutter" approach to forming an acceptable ISO, the requirement of fair and non-discriminatory rules of governance (Principle One) and the requirement that ISO employees have no financial interest in the economic interests of power marketers - - backed by strict conflict of interest provisions -- (Principle Two) are fundamental to our approving any ISO.

Pro Forma Tariff Provisions

The *pro forma* tariff is the basic mechanism implementing the requirements of comparable open access transmission. It **[30,180]** provides the details of the transmission service obligations imposed on jurisdictional utilities by the Rule. On rehearing we affirm most of the provisions set out in Order No. 888 for the *pro forma* tariff. We do make changes to conform the *pro forma* tariff to

changes adopted under other sections (for example, the definition of "eligible customer").

The rehearing petitions raised many questions about how particular aspects of the tariff will work. For the most part, these questions cannot be answered generically, but must be resolved on a case-by-case basis in the context of specific fact situations. However, the petitions brought to light issues that require clarifications and in some cases revisions to the tariff. The most significant of these involve discounting practices, provisions governing priority of service and curtailment, and the reciprocity provision.

Discounting practices. Originally, we provided different rules depending upon whether the transmission provider was offering a discount to itself or an affiliate or offering a discount to a non-affiliate. In response to the rehearing petitions, we are making three significant changes to the discounting requirements to better permit the ready identification of discriminatory discounting practices while also providing greater discount flexibility.

First, any discount offered on transmission services (including supporting ancillary services) by a transmission provider or requested by any customer must now be made only over the OASIS. With this change, all will have the same, timely access to discounted services. In making this change, we clarify that a transmission provider may limit its discounted service to particular time periods.

Second, once the provider and customer agree on a discount, the details of the discounted service -- the price,

points of receipt and delivery, and length of service -- must be immediately posted on the OASIS.

Third, we revise our Rule respecting what other transmission paths must be offered at a discount. Originally, in Order No. 888, we required that when a discount was offered over one path, the transmission provider would have to provide that discount over all other unconstrained paths on its system. We will no longer require this. Instead, the discount will be limited to those unconstrained paths that go to the same point(s) of delivery as the discounted service being provided on the transmission provider's system. The discount will extend for the same time period and must be offered to all transmission service customers.

Priority and Curtailment. We affirm the right of first refusal policy that reservation priority continues for firm service customers served under a contract of one year or more. We also affirm that curtailment must be made on a pro-rata basis and clarify that non-firm point-to-point service is subordinate to firm service. However, we clarify that the pro-rata curtailment requirement extends to only those transactions that alleviate the constraint.

Reciprocity. In Order No. 888 we conditioned the use of a public utility's open access service on the agreement that, in return, it is offered reciprocal service by non-public utilities that own or control transmission facilities. Such reciprocal service does not have to be through an open access tariff, i.e., a tariff available to all eligible customers, but may be limited to those public utilities from whom the non-public utility obtains open access service. We affirm the reciprocity

condition. In doing so, however, we make several clarifications.

First, a public utility is free to offer transmission service to a non-public utility without requiring reciprocal service in return. In other words, it may voluntarily waive the reciprocity condition. However, if it chooses to do so, transmission service must be provided through the pro forma tariff. Alternatively, bilateral agreements for transmission service provided by the public utility will not be permitted.

Second, we clarify that under the reciprocity condition a non-public utility must agree to offer the Transmission Provider any transmission service the non-public utility provides or is capable of providing on its system. This means that the non-public utility undertaking reciprocity must have an OASIS and must operate under the standards of conduct imposed under Order No. 889 unless it is granted a waiver by the Commission or, where appropriate, by a regional transmission group (RTG) of which it is a member. We also clarify that a non-public utility cannot avoid its responsibilities by **[30,181]** obtaining transmission service through other transmission customers. Further, the seller as well as the buyer in the chain of a transaction involving a non-public utility will have to comply with the reciprocity condition.

Third, we adhere to our decision not to treat generation and transmission (G&T) cooperatives and their member distribution cooperatives as a single unit. Thus, the reciprocity provision extends to the G&T Cooperative and not to its member distribution cooperatives.

Fourth, we clarify the "safe harbor" provision under which a non-public utility may get a Commission decision that its transmission tariff suffices to meet reciprocity. A non-public utility may limit the use of any reciprocity tariff that it voluntarily files at the Commission to those transmission providers from whom the non-public utility obtains open access service. A non-public utility also may satisfy reciprocity through bilateral agreements with a public utility. As a related matter, if a public utility believes a non-public utility is violating the reciprocity condition, it may file with the Commission a petition to terminate its service to the non-public utility.

Fifth, we clarify that non-public utilities may include stranded cost provisions in their reciprocity tariffs.

Sixth, the order on rehearing removes the term "interstate" from the reciprocity provisions. This is to make clear that reciprocity applies even to those who do not own or control interstate transmission facilities; *i.e.*, foreign utilities and those located in the ERCOT region of Texas.

As to local furnishing bonds held by some public utilities, we clarify that all costs associated with the loss of tax-exempt status of those bonds caused by providing open access transmission service are properly considered costs of providing that service. This includes costs of defeasing, redeeming, and refinancing those bonds.

Other Clarifications. In this order on rehearing we take the opportunity to clarify various other tariff provisions. Among these: Transmission providers do not have to take service under the open access tariff for transmitting power

purchased on behalf of their bundled retail customers. Also, the ability to reserve capacity to meet the reliability needs of a transmission provider's native load applies equally to present transmission and transmission that is built in the future.

Implementation

On rehearing, we make no substantive changes to the implementation provisions originally required under Order No. 888. For the most part, the implementation process has been completed. Utilities have made the requisite tariff and compliance filings and public and non-public utilities have, through other orders, been provided guidance as to obtaining waivers of Order No. 888 and Order No. 889 requirements.

We emphasize that we do not require the abrogation of existing contracts. Rather, the Rule requires only that transmission providers offer transmission under the open access tariff in addition to existing service obligations. Commitments made under existing contracts will continue. Of course, both transmission providers and their customers may seek to revise the terms and conditions of existing contracts by making the necessary filings, as appropriate, under Sections 205 or 206 of the Federal Power Act.

State and Federal Jurisdiction

On rehearing we reaffirm our decision that when transmission service is provided to serve retail customers apart from any contract for the retail sale of power, i.e., when it is provided on an unbundled basis, that transmission service is under our jurisdiction. In today's market, and increasingly

in the future as more states adopt retail wheeling programs, retail transactions are, and will be, broken down into products that are sold separately -- transmission and generation -- and sold by different entities. The exercise of our jurisdiction over the rates, terms and conditions of unbundled retail transmission will, therefore, become more important. We also recognize that states have jurisdiction over facilities used for local distribution.

On rehearing we also reaffirm the seven-factor test of Order No. 888 to distinguish transmission under our jurisdiction from state-jurisdictional local distribution. In doing so, we recognize that our test does not resolve all possible issues. There may be other factors that should be taken into account. The test, therefore, is designed for flexibility to include unique local characteristics and usages. To that end, we will continue to defer to state findings on these matters.

In addition, we clarify that states have the authority to determine the retail marketing areas of the electric utilities within their respective jurisdictions. We also recognize that states have the concomitant authority to determine the end user services these utilities provide.

Stranded Costs

On rehearing, we reaffirm our basic decisions surrounding the recovery of stranded costs. Utilities will be allowed the opportunity to seek to recover legitimate, prudent, and verifiable wholesale stranded costs. This opportunity is limited to costs associated with serving customers under wholesale requirements contracts executed on or before July

11, 1994 that do not contain explicit stranded cost provisions; and costs associated with serving retail-turned-wholesale customers.

We clarify that we will consider on a case-by-case basis whether to treat a contract extended or renegotiated without a stranded cost provision as an existing contract for stranded cost purposes.

In each case, the opportunity to seek stranded costs is limited to situations in which there is a direct nexus between the availability and use of a Commission-required transmission tariff and the stranding of the costs. The Rule does not allow the recovery of costs that do not arise from the new, accelerated availability of non-discriminatory transmission access.

The Commission also reaffirms its decision that stranded costs should be recovered from the customer that caused the costs to be incurred. The Commission is not requiring other remaining customers, or the utility, to shoulder a portion of its stranded costs that meet the requirements for recovery.

The Commission, as described in Order No. 888, will be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. With respect to such cases, we have made several changes.

First, the Commission has reconsidered its decision respecting cases involving existing municipal utilities that annex retail customer service territories. Under Order No. 888, we found that in such cases the Commission should not

be the primary forum for determining stranded cost recovery. On rehearing we now find that such cases should fall within our province.

Second, we clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers applies regardless of whether the customer or its new supplier is the one requesting and contracting for the transmission service. To this end, we have revised the definition of "wholesale stranded cost."

With respect to the recovery of stranded costs caused by unbundled retail wheeling, we affirm that the only circumstance in which we will entertain requests for these types of costs is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required. We clarify that if a state regulatory authority has in fact addressed such costs, regardless of whether it has allowed full recovery, partial recovery or no recovery, utilities may not apply to the Commission to recover stranded costs caused by the retail wheeling.

Other

In this section we resolve questions concerning our information reporting requirements, regional transmission groups, and the special situations posed by utilities in the Pacific Northwest and by federal power marketing and similar agencies. Here we make some minor clarifications but make no significant changes to Order No. 888.

We are not persuaded that the information reporting requirements need to be changed at this time. Finally, we reject arguments that would have us fix generically any particular rate methodology for providing open access transmission service under the *pro forma* tariff.

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[pp. 30,208 - 30,218]

[30,208]

The Commission's General Counsel Never Asserted, Or Even Suggested, That The Commission Does Not Have The Authority To Order Wheeling As A Remedy For Undue Discrimination

Union Electric spends several pages of its rehearing request asserting that the Commission's own General Counsel has acknowledged the limitations on the Commission's authority to order wheeling.[98] In particular, it points to a statement by a Commission OGC witness that "'if Congress intends for the Commission to be able to deal with transmission on its own motion and thereby go further than simply dealing with industry proposals,' Congress would need 'to include an affirmative statement somewhere in the Act that the Commission could require wheeling on its own motion.'"[99] This same statement was previously raised by EEI and previously addressed in Order No. 888. We do not

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[98]Union Electric at pp. 37-40.

[99]Union Electric at pp. 38-39.

disagree that this statement was made. However, it must be read in the context of the witness' entire testimony in which the witness stated *four* times the view that the case law supports the argument that the Commission has authority to order wheeling as a remedy for undue discrimination.[100] Indeed, contrary to Union Electric's assertion, the extensive legal analysis set forth by the Commission's witness supports the position relied upon in this proceeding.[101] Thus, viewed in

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[100]Hearings on H.R. 1301, H.R. 1543, and H.R. 2224 before the Subcommittee on Energy and Power of the House Committee on Energy and Commerce, 102d Cong., 1st Sess. (May 1,2 and June 26, 1991), Statement of Cynthia A. Marlette, Associate General Counsel, Federal Energy Regulatory Commission, Report No. 102-60 at p. 60 ("However, as discussed below, there are strong legal arguments that the Commission's obligation to protect against undue discrimination carries with it the authority to impose transmission requirements as a remedy for undue preference or discrimination." "As discussed below, although the case law in this area has been uncertain, in OGC's opinion there is a strong legal argument that the Commission can require transmission as a remedy for undue preference or undue discrimination."); at pp. 69-70 ("The weight of the limited case law, particularly the AGD opinion, supports authority to order wheeling as a remedy for undue discrimination where substantial evidence exists."); at p. 106 ("I believe that we have substantial authority under the existing case law to mandate access where necessary to remedy anticompetitive effects.").

[101]The statement quoted was preceded by a legal analysis of the Commission's authorities under then existing law, including section 206, and a statement that an examination of the Commission's full authorities might further open up the industry. Further, it was made in the context of case-by-case industry

the context of the witness' entire testimony, Union Electric's arguments to the contrary are unavailing. Moreover, nowhere did the witness ever suggest, as asserted by Union Electric, that FPA sections 205 and 206 could only be used "to eliminate unduly discriminatory terms in a wheeling arrangement voluntarily filed with the Commission."[102]

The Commission Has The Authority To Order Public Utilities To Make Rate Filings In This Proceeding

We reject Union Electric's argument that our requirement that Group 2 Public Utilities make section 205 filings is contrary to the voluntary filing scheme inherent in section 205. It is true that the Commission ordinarily cannot require a utility to make a section 205 filing. However, in this situation the section 205 filing was required as a remedy under section 206 of the FPA to establish rates for non-discriminatory open access transmission. Acting pursuant to section 206 of the FPA, we found that undue discrimination exists in the wholesale transmission of electric power and ordered the filing of non-discriminatory open access transmission tariffs to remedy this discrimination. Section 206 further requires that upon such a finding the Commission "shall determine the just and reasonable rate, charge, classification, rule, regulation, **[30,209]** practice, or contract to be thereafter observed and in force. . . ." Thus, we had the

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proposals and the Commission's inability to require case-by-case wheeling on its own motion. It did not address section 206 authority to remedy undue discrimination.

[102]Union Electric at p. 39. We note that Union Electric did not cite to any page or particular language to support its assertion.

authority to set the rates that would be observed and in force following the effectiveness of open access transmission and initially proposed to set rates for each public utility. However, rather than take this intrusive approach, which necessarily would have required a number of generic assumptions and resulted in less than public utility-specific rates, upon issuance of the Final Rule, we chose to permit these public utilities to make section 205 filings to propose their own rates for the services provided in the *pro forma* tariff.

The Commission's Prior Failure To Order Wheeling As A Remedy For Undue Discrimination Is Not Dispositive

After discussing several cases that it asserts address the Commission's authority to remedy undue discrimination, Carolina P&L declares that "[p]erhaps the strongest evidence that the Commission lacks the power to compel wheeling under FPA section 206 is the fact that the Commission has never previously exercised this alleged power, despite numerous opportunities to do so."[103] However, the court in AGD succinctly dismissed a similar argument:

> It is finally argued that the Commission's not having imposed any requirements like those of Order No. 436 in the period from enactment in 1938 until the present demonstrates the lack of any power to do so. . . . But as our introductory review of the economic background sought to illustrate, the Commission here deals with conditions that are

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[103]Carolina P&L at pp. 35-36.

> altogether new. Thus no inference may be drawn from prior non-use.[104]

Undue Discrimination/Anticompetitive Effects[105]

A number of utilities and state commissions argue that the Commission lacks evidence to support a finding of undue discrimination.[106]

VA Com argues that the Commission failed to make a legally supportable finding of industry-wide undue discrimination: "FERC apparently drew a conclusion that there was undue discrimination in the NOPR without support and later accepted customers' allegations, without further inquiry, and relied on them in making its finding of industry-wide undue discrimination." (VA Com at pp. 2-3).

PA Com and Carolina P&L assert that allegations of undue discrimination do not form a sufficient basis to compel a generic rulemaking. Not coming forward with specific

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[104]824 F.2d at 1001. In this regard, we acknowledge that our view of what constitutes undue discrimination has evolved significantly in light of the dramatic economic changes in the industry, as described briefly above and more fully in Order No. 888.

[105]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,682-84; *mimeo* at pp. 136-42.

[106]*E.g.*, El Paso, Union Electric, Carolina P&L, VA Com, FL Com, PA Com.

accusations and the identity of specific accusers, PA Com asserts, is unconstitutional as a deprivation of due process.

With regard to specific allegations of undue discrimination, SoCal Edison argues that the Commission inappropriately relied upon allegations involving SoCal Edison as evidence of undue discrimination. SoCal Edison asks that the Commission declare that it is not making a factual determination as to any particular allegation especially since prior to 1994 the Commission defined discrimination differently. Dalton similarly argues that the Commission has no basis for finding that Georgia Power Company is engaged in unlawful undue discrimination as to new or roll-over transmission services in the operation of the Integrated Transmission System in Georgia (ITS) under the ITS agreement. Moreover, Dalton argues, even if it is found that GPC acted in unduly discriminatory manner, it is not practical or lawful to order open access tariff for new and roll-over services.

Finally, Carolina P&L argues that the comparability standard does not eliminate the "requirement" that parties must be similarly situated before discrimination is present, and that the Commission has not provided factual support for its implicit finding that public utilities and their native load customers are similarly **[30,210]** situated to third parties. It cites *City of Vernon v. FERC*, 845 F.2d 1042 at 1045-46 (D.C. Cir. 1988), in support.

Commission Conclusion

As an initial matter, the Commission grants SoCal Edison's request for clarification that in Order No. 888 we

did not make a factual determination as to any particular allegation of past discrimination described in the Final Rule.[107] However, we reject arguments that the Commission cannot rely in part on the array of allegations and circumstances raised by customers in individual cases over the years and brought forth in response to the NOPR. The specific allegations are illustrative. However, they present examples of the types of discriminatory incentives and behavior inherent in ownership of monopoly transmission facilities, and also present credible examples of the types of discriminatory behavior in which public utilities could engage in the future. We also reject arguments that customers and the Commission must litigate and make specific findings of discrimination against each public utility before we can take any action to preclude discriminatory behavior that will harm competition and, ultimately, electricity consumers. This is particularly true where the discriminatory behavior clearly is in the economic self-interest of a monopoly transmission owner facing the markedly increased competitive pressures that are driving today's electric utility industry. As we recognized in Order No. 888,

> [t]he inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by

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[107]In response to PA Com's and Carolina P&L's assertions that not coming forward with specific accusations and identities of specific accusers is unconstitutional and a deprivation of due process, we emphasize that the Commission has not denied due process to anyone. The Final Rule does not, nor is it intended to, make specific findings as to any particular utility or any particular allegation raised.

> refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own generation, and it is our duty to eradicate unduly discriminatory practices. As the AGD court stated: "Agencies do not need to conduct experiments in order to rely on the prediction that an unsupported stone will fall."[108]

We believe that the same general discriminatory circumstances that faced us when we required open access transportation in the natural gas industry[109] are also before us today in the electric industry. First, it is uncontested that market power continues to exist in the ownership and operation of the monopoly-owned facilities that comprise the nation's interstate transmission grid. Second, utilities, as a general matter, did not in the past offer comparable transmission services to competitors or to customers. Open access services simply were not made available by utilities until the late 1980s when the Commission began to impose open access as a condition of approval of market-based rates and utility mergers in order to mitigate market power and remedy anticompetitive effects. Rather, the vast majority of utilities historically have declined to transport electric energy that would compete with their own sales or have offered access that is inferior to what they use for their own sales. Third, discrimination in transmission services, when viewed in light of utilities' own uses of their transmission systems

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[108] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 331,682; *mimeo* at pp. 136-37.

[109] *See AGD*, 824 F.2d at 999-1000.

compared to what they offer third parties, has denied and will continue to deny customers access to electricity at the lowest reasonable rates. The entities on rehearing have raised nothing to persuade us that it is in the interests of consumers to maintain the self-evident incentives for transmission owners to exercise their monopoly power over transmission to discriminate in favor of their own generation sales -- incentives that will only increase in the future as competitive pressures continue to escalate.

The Commission addressed the same argument as that being made by Carolina P&L, that the Commission has not made the requisite finding that third-party transmission customers are similarly situated to public utilities and their native load customers, in 1994 in the *NEPOOL* **[30,211]** and *AEP* cases.[110] In these cases, we recognized that the traditional focus of our undue discrimination analysis had been whether factual differences justify different rates, terms and conditions for similarly situated customers, but concluded that due to changing conditions in the electric utility industry, it was necessary to reevaluate our traditional analysis. As we stated in *NEPOOL*, the focal point of undue discrimination claims has shifted from claims of undue discrimination in rates and services which the utility offers different customers to claims of undue discrimination in rates and services which the utility offers when compared to its own use of the transmission

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[110]*New England Power Pool*, 67 FERC ¶61,402 (1994) (*NEPOOL*); *American Electric Power Service Corporation*, 64 FERC ¶61,279 (1993), *reh'g granted*, 67 FERC ¶61,168, *clarified*, 67 FERC¶61,317 (1994) (*AEP*).

system.[111] "In this context, framing the analysis in terms of how a public utility treats similarly situated customers is not applicable or instructive."[112] The Commission concluded that it therefore must reexamine its application of the standard for undue discrimination claims under sections 205 and 206 of the FPA. The Commission further elaborated on its re-examination of undue discrimination in AEP. The Commission cited its NEPOOL discussion and set for hearing the different uses that AEP made of its transmission system and whether there were any operational differences between any particular use that AEP made of the system and the use third parties might need, and, in particular, the degree of flexibility AEP accorded itself in using its transmission system for different purposes. The Commission subsequently set the same issue for hearing in several other cases.[113] In the NOPR, however, the Commission concluded that based on what it had learned in the ongoing cases, it would address this issue generically in this rulemaking. We announced in the NOPR our belief that all utilities use their own systems in two basic ways: to provide themselves point-to-point transmission service that supports coordination sales, and to provide themselves network transmission service that supports the economic dispatch of their own generation units and purchased power resources (integrating their resources to meet their internal load). Third parties may need one or both

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[111] 67 FERC ¶61,042 at p. 61,132.

[112] *Id.*

[113] *Commonwealth Edison Co.*, 70 FERC ¶61,204 (1995); *Wisconsin Electric Power Co.*, 70 FERC ¶61,074 (1995); and *Wisconsin Public Service Corp.*, 70 FERC ¶61,075 (1995).

of these basic uses in order to obtain competitively priced generation or to have the opportunity to be competitive sellers of power, and the Commission proposed that all public utilities must offer both services on a non-discriminatory open access basis.[114]

We affirmed this determination in the Final Rule. We concluded that a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others. Because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today.[115] Thus, based on the analysis in this record, the Commission has determined that undue discrimination in the provision of transmission services in today's industry does not turn on whether utilities and their native load customers are similarly situated to third parties, but instead turns on whether the utility is providing comparable service, that is, service that it is reasonably capable of providing to other users of the interstate transmission system.

In short, the Commission is not bound to a static application of its undue discrimination analysis under the FPA and, indeed, has a public interest responsibility to reexamine undue discrimination in light of changed circumstances in the

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[114]*FERC Statutes and Regulations* ¶32,524 at p. 33,079.

[115]*FERC Statutes and Regulations* at p. 31,690; *mimeo* at p. 160.

industry.[116] That is what we began in NEPOOL and AEP and have completed in this rulemaking. The traditional "similarly **[30,212]** situated" test, while applicable to discrimination among third-party customers, simply is not applicable when analyzing discrimination between third-party transmission customers and transmission owners. Under Carolina P&L's theory, presumably the only customers that could be shown to be similarly situated would be those who own monopoly transmission facilities and have native load (i.e., captive) customers. This would preserve customer captivity, perpetuate monopoly power and profits, and deny the lowest reasonable rates to consumers. We therefore reject Carolina P&L's arguments.

Moreover, the fact that public utilities and their native load customers have been treated differently from third-party transmission customers because they are not among those traditionally considered to be "similarly situated" is precisely the target at which Order No. 888 takes aim. Historically, competitively-priced power was not broadly available to wholesale customers because the industry was dominated by

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[116]There is no "requirement" in the FPA that the Commission apply a "similarly situated" test. Carolina P&L's reliance on City of Vernon is misplaced. That case involved a claim of discrimination in the type of service offered to a wholesale customer versus that offered to retail customers, and the Commission's application of the "similarly situated" and "same service" test. Contrary to Carolina P&L's implication, the case does not hold that the Commission is bound to apply a "similarly situated" test in analyzing undue discrimination claims under the FPA.

vertically integrated IOUs[117] and, to the extent cheaper generation alternatives were available in the marketplace, transmission owners either took the cheaper power for their own uses or purchased and re-sold it at a profit.[118] Prior to EPAct, most power customers took power from the vertically integrated utilities that provided their transmission service. Transmission-only transactions played a secondary role in bulk power markets, facilitating certain economy transactions and coordination and pooling arrangements that improved utility operational efficiencies, largely as a complement to bundled bulk power transactions. Given the predominantly vertically-integrated industry and efficiencies that could be gained through encouragement of coordination and pooling transactions, the Commission was willing to accept utility practices that provided third parties with transmission services that were distinctly inferior to the utility's own uses of the transmission system.

In the future, however, unbundled transmission service will be the centerpiece of a freely traded commodity market in electricity, in which all wholesale customers can shop for power. In a market characterized by a significant increase in

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[117]I.e., investor-owned utilities that owned generation, transmission and distribution facilities and most of whom had captive customers.

[118]Very simply, the transmission owner was able to prevent third parties from achieving the maximum savings possible in the generation market by withholding or delaying transmission service. Alternatively, the transmission owner could purchase the power and resell it to the third party at a rate that reflected a mark-up from the first power sale.

non-vertically integrated power suppliers and competitively priced power that is now meaningfully available, it is no longer in the interest of wholesale customers for the Commission to tolerate the types of practices that were previously accepted. We cannot allow what have become unduly discriminatory practices to erect barriers between customers and the rapidly emerging competitive electricity marketplace. Accordingly, a primary goal of Order No. 888 is to provide that in the future transmission providers and third-party transmission customers are "similarly situated" in the quality of transmission service available to them.

C. Comparability

1. Eligibility to Receive Non-discriminatory Open Access Transmission

In the Final Rule, the Commission modified the definition of "eligible customer" and, among other things, clarified that any entity engaged in wholesale purchases or sales of electric energy, not just those "generating" electric power, is eligible.[119] The Commission also clarified that entities that would violate section 212(h) of the FPA (prohibition on Commission-mandated wheeling directly to an ultimate consumer and sham wholesale transactions) are not eligible. Further, the Commission clarified that foreign entities that otherwise meet the eligibility criteria may obtain transmission services. The **[30,213]** Commission also provided for service to retail customers in circumstances that

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[119]*FERC Statutes and Reuglations, Regulations Preambles January 1991-June 1996* at pp. 31,688-90; *mimeo* at pp. 154-58.

do not violate FPA section 212(h). Persons that would be eligible section 211 applicants also would be eligible under the open access tariff.

a. Unbundled Retail Transmission and "Sham Wholesale Transactions"

Rehearing Requests

Several entities assert that there is an inconsistency between tariff language and preamble language and argue that section 1.11 of the tariff should be made consistent with the preamble to ensure that, absent a state-approved program, retail wheeling is not available under the tariff, no matter which party requests service.[120] They maintain that the limitation in section 1.11 that the transmission provider only must provide retail transmission service voluntarily or under a state-approved program appears to apply only when a retail customer is the purchaser, not when the transmission purchaser is an electric utility. They suggest the following language to remedy the problem: "however, such entity is not eligible for transmission service that would be prohibited by Sections 212(h)(1) and/or 212(h)(2) of the Federal Power Act, unless such service is provided pursuant to a state retail access program or pursuant to a voluntary offer of unbundled retail transmission service by the Transmission Provider." (PSE&G at p. 22; Carolina P&L at pp. 8-9).

Detroit Edison argues that the Commission should modify the definition to exclude any reference to transmission

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[120] *E.g.*, SoCal Edison, PSE&G, Carolina P&L.

service provided to retail customers so as to avoid confusion and possible forum shopping. At the least, Detroit Edison argues, the Commission should modify the language to state that transmission service is available to an ultimate consumer to the extent, and only to the extent, that the service is authorized by a lawful state retail access program or pursuant to a voluntary offer of unbundled retail transmission service by the transmission provider.

NYSEG asserts that the Commission did not apply the section 212(h) limitation to service to retail customers under the tariff. NYSEG requests that the Commission clarify that it will not require retail wheeling beyond the scope of state-mandated retail access programs or beyond the terms of a transmission provider's voluntary offer of retail wheeling service.

Oklahoma G&E asks the Commission to clarify that the term eligible customer differentiates between a customer eligible to receive transmission service and a customer whose transaction is a sham or would result in mandatory retail wheeling and would therefore be prohibited by section 212(h).

NYSEG further asserts that the right of first refusal provision would permit a retail customer receiving wheeling service to continue to take that service upon expiration of its contract, which could require the transmission provider, in violation of section 212(h), to continue retail wheeling beyond the scope of its voluntary offer of service or beyond the scope of a state-mandated retail access program.

SoCal Edison argues that the Commission cannot compel a utility to supply retail transmission service if the

utility challenges the authority of the state to require retail wheeling and section 1.11 should be revised to reflect this.

IL Com declares that it "does not recognize FERC's claim of jurisdiction over retail transmission service provided directly to a retail customer and disputes that unbundled retail wheeling directly to a retail customer is a service provided in interstate commerce." (IL Com at 35). Thus, "if FERC's proposed 'deference' to states is to be given any effect, states must be allowed to determine whether the retail transmission component of the retail wheeling program will be provided pursuant to the utility's existing filed wholesale tariff or whether the retail transmission will be provided pursuant to a 'separate retail transmission tariff' that is different from the wholesale tariff." (IL Com at 36). IL Com concludes that it is inappropriate (and illegal if FERC is overturned on its retail transmission jurisdiction assertion) to include retail customers taking final delivery of unbundled power for their own end uses under retail wheeling programs as eligible customers.

[30,214]

PA Com argues that it is relevant whether a customer is receiving retail or wholesale service and redefining transmission and local distribution service does not automatically convey jurisdiction to the Commission.

CCEM asks that the Commission clarify that a retail customer eligible to seek transmission service should be able to seek transmission service not only from the transmission provider, but from any other transmission provider. CCEM also asks that the Commission add the word "ultimate" before the word transmission provider in section 1.11 of the tariff.

EEI asks the Commission to "clarify that the transmission service provider should be allowed to supplement the terms and conditions of the *pro forma* tariff with additional provisions that specifically relate to the totality of the transmission service being provided, including the use of distribution facilities and any other transmission facilities not currently included in wholesale rates." (EEI at p. 24 (emphasis in original)).[121]

Union Electric argues that a literal reading of the eligibility definition could require retail wheeling by utilities in states other than those required to participate in a particular retail wheeling program.

Commission Conclusion

The Commission agrees with those entities that argue that section 1.11 of the pro forma tariff does not explicitly prohibit "sham wholesale transactions" that could currently be arranged under the tariff by a utility applying for service and designating the retail customer as a point of delivery. We therefore have modified section 1.11 to clarify that, with respect to service that we are prohibited from ordering by section 212(h) of the FPA (whether direct retail wheeling or "sham" wholesale wheeling), otherwise eligible entities may obtain such service under the tariff only if it is pursuant to a state requirement that such service be provided or pursuant to a voluntary offer of such service. We also have modified the language to clarify that eligibility for unbundled direct retail service required by a state applies only to service from

[121]See also *CSW Operating Companies*.

transmission providers that the state orders to provide the service. The modified language states:

> Eligible Customer: (i) Any electric utility (including the Transmission Provider and any power marketer), Federal power marketing agency, or any person generating electric energy for sale for resale is an eligible customer under the tariff. Electric energy sold or produced by such entity may be electric energy produced in the United States, Canada, or Mexico. However, with respect to transmission service that the Commission is prohibited from ordering by Section 212(h) of the Federal Power Act, such entity is eligible only if the service is provided pursuant to a state requirement that the Transmission Provider offer the unbundled transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider. (ii) Any retail customer taking unbundled transmission service pursuant to a state requirement that the Transmission Provider offer the transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider, is an eligible customer under the tariff.

Regarding SoCal Edison's argument, the Commission stated in the Final Rule:

> Moreover, we are mindful of the fact that we are precluded under section 212(h) from

> ordering or conditioning an order on a requirement to provide wheeling directly to an ultimate consumer or sham wholesale wheeling. We therefore clarify that our decision to eliminate the wholesale customer eligibility requirement does not constitute a requirement that a utility provide retail transmission service. Rather, we make clear that if a utility chooses, or a state lawfully requires, unbundled retail transmission service, such service should occur under this tariff unless we specifically approve other terms.[122]

Therefore, the Commission is not compelling a utility to provide unbundled retail transmission service.[123] Rather, the Commission **[30,215]** requires that should such service be provided, either pursuant to state mandate or voluntarily, it must be provided pursuant to the pro forma tariff unless the Commission approves alternative terms and conditions.

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[122]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,689-90; *mimeo* at p. 158.

[123]We also disagree with NYSEG's assertion that the right of first refusal provision would permit a retail customer receiving wheeling service to continue to receive service after the expiration of its contract and could require the transmission provider to continue wheeling beyond the scope of its voluntary offer of service or beyond the scope of a state-mandated retail access program. Section 212(h) of the FPA would override any provision, including the right of first refusal provision, that may be included in the pro forma tariff.

However, in light of CCEM's request that we clarify that a retail customer eligible to seek transmission service under the tariff should be able to seek service not only from the transmission provider, but also from any other transmission provider, and in light of Union Electric's concerns regarding retail service eligibility, we believe certain clarifications of our jurisdiction and of the statements made in Order No. 888 are necessary. The statements cited above that were made in Order No. 888 and the eligible customer tariff definition in (ii) above refer to direct retail transmission, i.e., the transmission of electric energy "directly" to an ultimate consumer. The Commission is prohibited by section 212(h)(1) of the FPA from ordering this type of retail transmission and that is why customers are eligible for such transmission under the tariff only if the transmission is pursuant to a state order or is provided voluntarily. However, on its face, section 212(h) does not prohibit the Commission from ordering public utilities to provide "indirect" unbundled retail transmission in interstate commerce, i.e., the transmission necessary to transmit unbundled electric energy to a utility that ultimately will deliver the energy to a customer that is purchasing the unbundled energy at retail either pursuant to a state retail access order or pursuant to voluntary delivery by the local utility.

We clarify that we believe we have the jurisdiction under the FPA to order indirect retail transmission to an ultimate consumer and that if the Commission under sections 205, 206 or 211 of the FPA orders such transmission, entities that otherwise qualify as eligible customers under the tariff will take transmission service for such indirect retail wheeling pursuant to the *pro forma* tariff. We note that the Commission may order such transmission on a case-by-case basis or may

determine to do so generically in the future. We expect public utilities to provide such indirect retail access under the *pro forma* tariff and, if they do not, we will not hesitate to order them to do so.

In response to IL Com's argument that it does not recognize this Commission's claim of jurisdiction over the rates, terms and conditions of unbundled retail transmission that is provided directly to an ultimate consumer, the Commission reaffirms its legal conclusion set forth in the Final Rule.[124] As to its claim that we should give deference to the state as to whether such service could be taken under the wholesale tariff or a separate retail tariff on file with the Commission, we reaffirm our conclusion to address this on a case-by-case basis. Since the Final Rule issued, the Commission has addressed this in several orders. In New England Power Company, the Commission stated:[125]

> As we explained in the Open Access Rule and in the New Hampshire Interim Order, we generally expect retail transmission customers to take service under the same Commission tariff that applies to wholesale customers.

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[124] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,780 and appendix G (at pp. 31,966-81); *mimeo* at p. 428 and appendix G.

[125] 75 FERC ¶61,356 at p. 62,141, *order on reh'g*, 77 FERC ¶61,135 (1996). In the order on rehearing, the Commission permitted a separate retail tariff to remain in effect for the duration of the retail electric pilot programs established in Massachusetts by Massachusetts Electric Company.

> While we generally will defer to state requests for a separate retail tariff to accommodate the design and special needs of a state retail access program, the Massachusetts Commission has made no such request in this case.[15]

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[15] See Open Access Rule, *FERC Statutes and Regulations*, at p. 31,784; *New Hampshire Interim Order*, 75 FERC at p. 61,687 & n.3 (both noting that such a separate retail tariff must **[30,216]** be consistent with the Commission's open access policies and comparability principles). . . .

Subsequently, in New England Power Company, 76 FERC ¶61,008 (1996), the Commission granted a limited waiver of the Open Access Rule requirements for the New Hampshire retail electric competition pilot project. Specifically, the Commission waived the requirement for individual service agreements, and the requirement for customer deposits. The Commission further announced that:

> other public utilities that provide unbundled retail service under a *pro forma* tariff do not need to apply to retail customers the tariff provisions regarding individual service agreements or customer deposits, unless a state retail program so requires.[126]

Concerning EEI's request for clarification, the Commission stated in the Final Rule:

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[126] 76 FERC at p. 61,024.

> all tariffs need not be "cookie-cutter" copies of the Final Rule tariff. Thus, under our new procedure, ultimately a tariff may go beyond the minimum elements in the Final Rule pro forma tariff or may account for regional, local, or system-specific factors. The tariffs that go into effect 60 days after publication of this Rule in the Federal Register will be identical to the Final Rule pro forma tariff; however, public utilities then will be free to file under section 205 to revise the tariffs, and customers will be free to pursue changes under section 206.[127]

Utilities are free to include customer-specific terms and conditions or terms and conditions limited to certain customers (*e.g.*, a distribution charge) in the customer's service agreement and/or the network customer's network operating agreement.

b. Transmission Providers Taking Service Under Their Tariff

Rehearing Requests

TAPS states that section 1.11 does not seem to require a transmission provider to take service for its purchases, but the preamble does (citing mimeo at 57, 191, 266 and

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[127] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,770 n. 514; *mimeo* at p. 399 n. 514.

regulatory text in section 35.28(c)(2)). It argues that transmission providers should be required to treat their own usage of the transmission system to serve retail customers under the network service provisions of the tariff. TAPS argues that this result could be achieved through an ISO or by requiring transmission providers to abide by all non-price terms of Parts I and III of the tariff. TAPS also argues that the rates charged network customers must be developed on the same basis as the transmission component of retail rates. It states that the transmission provider's purchases would then be made under Part III of the tariff to the extent they are made for serving retail customers. It further asserts that the Commission's authority and obligation to consider transmission owners' service to retail load in establishing wholesale transmission rates has been long established. At the least, TAPS argues that the Commission should require that a transmission provider take its wholesale purchases under some tariff.

Similarly, Coalition for Economic Competition asks the Commission to clarify that the requirement to use the *pro forma* tariff for wholesale purchases and to functionally unbundle wholesale purchases and sales does not apply to purchases made solely to serve retail customers on a bundled basis. It asserts that there is conflicting language in Order No. 888 (citing *mimeo* at p. 191) and Order No. 889 (citing *mimeo* at p. 12) and the *pro forma* tariff. Coalition for Economic Competition asserts that the Commission does not have jurisdiction over transmission that is part of a bundled retail sale.

Commission Conclusion

Several parties have noted on rehearing that there is conflicting language among the Final Rule, Order No. 889 and the *pro forma* tariff as to whether and to what extent the transmission provider must take service for "wholesale purchases" under its own tariff. As discussed below, we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power **[30,217]** that is purchased on behalf of bundled retail customers.

In a situation in which a transmission provider purchases power on behalf of its retail native load customers, the Commission does not have jurisdiction over the transmission of the purchased power to the bundled retail customers insofar as the transmission takes place over such transmission provider's facilities,[128] and therefore the pro forma tariff does not have to be used for such transmission. Moreover, we recognize that purchases made collectively on behalf of native load[129] cannot necessarily be identified as

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[128]To the extent the transmission takes place on the interstate facilities of other public utilities, we would have jurisdiction over such transmission.

[129]Native load means "[t]he wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers." Section 1.19 of the *pro forma* tariff.

going to any particular customer. However, the Commission does have jurisdiction over transmission service associated with sales to any person for resale, and such transmission must be taken under the transmission provider's pro forma tariff.[130]

Order No. 888, relying on the principle of comparability, established the terms and conditions for network service provided to network customers under the *pro forma* tariff. Network customers may include the transmission provider itself as well as any other entity receiving Network Integration Service. If the transmission provider purchases energy from another power supplier in order to make sales to its wholesale native load customers, it must take the transmission service necessary to transmit the power from its point(s) of receipt to its point(s) of delivery under the same terms and conditions as other Network Customers.[131] As we explained in *AES Power, Inc.*, network customers are entitled to make economy energy purchases from non-designated network resources at no additional charge on a basis

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[130]All transmission in interstate commerce by a public utility in conjunction with a sale for resale of electric energy is jurisdictional and must be taken under a FERC-jurisdictional tariff. The same is true for all unbundled transmission in interstate commerce to wholesale customers, as well as to unbundled retail customers.

[131]Under the Order No. 888 pro forma tariff, third-party wholesale customers have the ability to obtain the identical service the transmission provider provides itself when it engages in a sale of electric energy for resale. This may include network or point-to-point service.

comparable to the economy energy purchases made by the transmission provider on behalf of its bundled retail customer.[132] This applies to the transmission provider as a network transmission customer under its own tariff as well as to other network transmission customers that make economy energy purchases on behalf of their customers. Thus, insofar as all wholesale transmission customer usage is concerned, third-party network customers are treated the same as the transmission owner.

2. Service that Must be Provided by Transmission Provider

In the Final Rule, the Commission found that a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others.[133] The Commission explained that because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today. However, the Commission explained that if a customer seeks a customized service not offered in an open access tariff, a customer may, barring successful negotiation for such service, file a section 211 application.

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[132]69 FERC ¶61,145 at p. 62,300 (1994) (proposed order), 74 FERC ¶61,220 (1996) (final order).

[133]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,690; *mimeo* at p. 160.

Rehearing Requests

Cleveland requests that the Commission make explicit that comparability will be evaluated not only by reference to a transmission provider's wholesale services, but also by comparison to the terms, conditions, and prices applicable to **[30,218]** its retail services, whether bundled or unbundled. Cleveland asserts that this is needed so that TDUs are not at a competitive disadvantage in competing with the transmission provider for retail customers. It maintains that this is consistent with the Transmission Pricing Policy and established precedent.

Commission Conclusion

No clarification is necessary. In determining what transmission services a utility must offer for wholesale sales of electric energy in interstate commerce, the Final Rule explicitly states that "a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others."[134] Further, the Final Rule requires that network service customers receive service comparable to the service provided to the transmission provider's native load. Because the Rule applies to retail transmission that is voluntarily offered or pursuant to a state retail access program, the requirements to offer services that the utility is reasonably capable of providing and services comparable to those

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[134] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996 at p. 31,690; mimeo at p. 160.*

provided to native load would also apply to retail service in these limited retail circumstances.

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[pp. 30,278 - 30,279]

[30,278]

3. Curtailment and Interruption Provisions[297]

a. Pro-Rata Curtailment Provisions

In the Final Rule, the Commission found that curtailment on a pro-rata basis is appropriate for curtailing transactions that substantially relieve a constraint.[298] The Commission explicitly allowed the transmission provider discretion to curtail the services, whether firm or non-firm, that substantially relieve the constraint.

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[297]In the Final Rule *pro forma* tariff, the Commission defines curtailment as: "A reduction in firm or non-firm transmission service in response to a transmission capacity shortage as a result of system reliability conditions." (pro forma tariff section 1.7). The *pro forma* tariff defines interruption as: "A reduction in non-firm service due to economic reasons pursuant to Section 14.7." (*pro forma* tariff section 1.15). The distinction between curtailment and interruption may have been blurred in Order No. 888 and this order attempts to clarify that distinction.

[298]*FERC Statutes and Regulations, Regulation Preambles January 1991-June 1996* at p. at 31,749; *mimeo* at pp. 335-36.

The Commission also indicated that it would consider granting deference to an alternative curtailment method to avoid hydro spill if such a regional practice is generally accepted and adhered to across the region.

The Commission further found that under network and point-to-point service, the transmission provider may propose a rate treatment (penalty provision) to apply in the event a customer fails to curtail service as required under the Final Rule pro forma tariff and indicated that such proposals will be evaluated on a case-by-case basis on compliance.

Rehearing Requests

PA Com asserts that pro rata curtailment fails to hold native load harmless to the extent practical as required by the FPA. PA Com points out that on January 19, 1994, PJM initiated pro-rata load shedding, in part to preserve economic transactions, leaving customers in Pennsylvania without power during a record cold spell.

VA Com argues that pro rata curtailment may harm native load customers and section 206 complaints are after the fact and of little assistance to native load. VA Com argues that curtailment priority (in order of curtailment) should be: non-firm, contract firm, and then native load, and that utilities should have flexibility to curtail on a pro-rata basis within classes, subject to state curtailment policy.

Several entities argue that provision must be made for preference in curtailment priorities obtained through settlement, through payment of good and valuable

consideration, or under existing transmission contracts.[299] Turlock argues that customers should be able to obtain a variation from the pro rata scheme if they can show that they have made either past or future investments to improve constrained facilities and that the quid pro quo for their investment is improved curtailment priority.

Allegheny asks the Commission to clarify that it did not intend to require public utilities to shed (through pro rata curtailment) native transmission load customers in order to preserve some portion of service to through system users of the grid. According to Allegheny, the FPA mandates that service reliability to franchise customers must be maintained and through-system users are not similarly situated to native transmission load customers and should not be treated the same in an emergency because through system customers can protect themselves, but native transmission load customers cannot. Allegheny adds that failure to maintain system reliability would violate section 211 of the FPA.

CCEM asserts that hard and fast priority rules are needed to prevent inconsistent rules from developing for different utilities, pools, or control areas.

Commission Conclusion

Assertions that the pro-rata curtailment provision in the tariff may harm native load customers are misplaced. The Commission clarified in the Final Rule that it was not requiring a pro-rata curtailment of all transactions at the time

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[299] *E.g.*, Santa Clara, Redding, TANC.

of a constraint, but rather curtailment of **[30,279]** those transactions, whether firm or non-firm, that effectively relieve the constraint.[300] The Commission also required that such curtailments be made on a non-discriminatory basis, including the transmission provider's own wholesale use of the system. The Commission further explained that the pro-rata curtailment provision was intended to apply to situations where multiple transactions could be curtailed to relieve a constraint. Of course, if curtailment of multiple transactions is necessary, non-firm service would be curtailed prior to firm service. However, the Commission established that, in emergencies, the transmission provider had the discretion to interrupt firm service under the tariff to ensure the reliability of its transmission system.

In terms of reliability, we believe that sufficient safeguards have been established to protect native load. In particular, the transmission provider is responsible for planning and maintaining sufficient transmission capacity to safely and reliably serve its native load. Order Nos. 888 and 889 permit the transmission provider to reserve, in its calculation of ATC, sufficient capacity to serve native load.

Allegations that a utility did not curtail on a non-discriminatory basis, but instead favored a certain class of customer or type of transaction should be filed in a section 206 complaint proceeding to be reviewed on a case-specific basis. While it is true that such complaints will be processed

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[300] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,749; *mimeo* at p. 335.

on an after-the-fact basis, it is only on a fact-specific basis that such complaints can be fully and adequately reviewed.

Additionally, tariff section 14.7 does in fact establish that for curtailment purposes, non-firm point-to-point transmission shall be subordinate to firm transmission service and non-firm service may also be interrupted for economic reasons. However, adopting curtailment schemes based solely on classes of service, as proposed by the VA Com, is inappropriate. Specifically, VA Com's proposal to curtail all non-firm transmission transactions prior to firm transactions could exacerbate an emergency situation. For example, a curtailment could be necessary due to a constraint affecting northbound transactions. However, curtailing all non-firm transactions, including southbound transactions (or counterflows), could worsen the situation. Accordingly, the Commission believes the approach established in the Final Rule of allowing non-discriminatory curtailments of the transaction(s) that effectively relieve(s) the constraint is appropriate.

In response to CCEM's concerns regarding the potential for inconsistent rules for different utilities, pools or control areas, the Commission explained in the Final Rule that any proposed deviations from the non-price terms and conditions of the pro forma tariff, such as regional practices, must be adequately supported by the utility proposing the change.

Finally, Order No. 888 did not abrogate existing contracts;[301] therefore, customers with unique curtailment priorities established by pre-existing contracts would not have these priorities eliminated for the term of the existing contract.

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[pp. 30,334 - 30,350]

[30,334]

I. Federal and State Jurisdiction: Transmission/Local Distribution

In the Final Rule, the Commission explained that after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both the initial Stranded Cost NOPR and in the Open Access NOPR, and the comments received on that analysis, it reaffirmed its **[30,335]** assertion of jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction.[451] The Commission also reaffirmed and clarified its determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in

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[301] We note that in Order No. 888 we partially modified existing economy energy coordination agreements. *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,666; *mimeo* at p. 91.

[451] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,780-85; *mimeo* at pp. 427-42.

situations involving unbundled wholesale wheeling and unbundled retail wheeling.

The Commission also explained that where states unbundle retail sales, it will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed by the Commission. In addition, the Commission clarified that there is an element of local distribution service in any unbundled retail transaction, and further clarified other aspects of its jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

The Commission reaffirmed its legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. The Commission found compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.

The Commission further explained that when a retail transaction is broken into two or more products that are sold separately, the jurisdictional lines change. In this situation, the Commission emphasized that the state clearly retains jurisdiction over the sale of the power, but the unbundled transmission service involves only the provision of

"transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission.

The Commission recognized that in asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, it was in no way asserting jurisdiction to order retail transmission directly to an ultimate consumer. It explained that its assertion of jurisdiction is that if unbundled retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission further clarified that nothing in its jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. It explained that while its jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over transmission in interstate commerce by public utilities.

The Commission also adopted a new section 35.27(b) as follows:

> Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority may have under applicable state and federal law, or (ii)

> limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non- discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities **[31,336]** are state-jurisdictional local distribution facilities, the Commission concluded that it could not divine a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. The Commission added that the limited case law, including *Connecticut Light & Power Company v. FPC (CL&P)* and *Federal Power Commission v. Southern California Edison Company* (the *Colton* case),[452] supports a case-by-case determination.[453] Accordingly, the

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[452]324 U.S. 515 (1945) (*CL&P*); 376 U.S. 205 (1964) (*Colton*).

[453]The Commission included a detailed legal analysis in Appendix G to Order No. 888. The Commission explained that it was particularly persuaded by the Supreme Court's statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. *See CL&P*, 324 U.S. at 534-35).

Commission stated that its technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

The Commission made two clarifications regarding local distribution in the context of retail wheeling. First, it explained that even if its technical test for local distribution facilities were to identify no local distribution facilities for a specific transaction, states have authority over the service of delivering electric energy to end users. Second, the Commission explained that through their jurisdiction over retail delivery services, states have authority not only to assess retail stranded costs but also to assess charges for so-called stranded benefits, such as low-income assistance and demand-side management.

Thus, under this interpretation of state/federal jurisdiction, the Commission explained, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

The Commission further determined that it is appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs.

In instances of unbundled retail wheeling that occurs as a result of a state retail access program, the Commission indicated that it will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for

local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[454] Moreover, the Commission indicated that it will consider jurisdictional recommendations by states that take into account other technical factors that the state believes are appropriate in light of historical uses of particular facilities.

As a means of facilitating jurisdictional line-drawing, the Commission stated that it will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, the Commission explained that, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission indicated that it will defer to such classifications and/or cost allocations.

Furthermore, the Commission stated that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances. The Commission

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[454]In order to give such deference, the Commission noted its expectation that state regulators will specifically evaluate the seven indicators and any other relevant facts and make recommendations consistent with the essential elements of the Rule.

explained that when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes -- a transmission component and a local distribution component. It again emphasized that the Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component. Thus, the Commission stated, **[30,337]** the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. However, the Commission added, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[455] to accommodate the design and special needs of such programs. In such situations, the Commission indicated that it will defer to state requests for variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by the Final Rule. In addition, the Commission indicated that the rates must be consistent with its Transmission Pricing Policy Statement, and the guidance set forth in Order No. 888 concerning ancillary services.[456]

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[455]The Commission noted that such a tariff could be different from the tariff that applies to wholesale customers, but that such tariff would still be filed with the Commission under FPA section 205.

[456]In applying the principles of the Final Rule to retail transmission tariffs, the Commission emphasized that it clearly cannot order retail wheeling directly to an ultimate consumer. (citing FPA section 212(h)).

The Commission also expressed concern, just as it did with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, the Commission reaffirmed its conclusion that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. Moreover, the Commission indicated that it will address these transactions on a case-by-case basis.

Rehearing Requests

Oppose Commission Assertion of Jurisdiction Over Unbundled Retail Transmission

Several state commissions indicate that, recognizing that the case law is not dispositive concerning the question of unbundled retail transmission services (either because the cases do not involve the transmission of power to retail customers or "fence off" local distribution from federal regulation), at least one court (*Wisconsin-Michigan Power Company v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert. denied*, 345 U.S. 934 (1953)) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services.[457] Thus, they argue, the Commission should apply the wholesale versus retail analysis to the question of unbundled retail transmission.

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[457] *E.g.*, NARUC, WI Com, WY Com.

IL Com asserts that retail transmission by a public utility directly to an end user has always (even before the FPA was enacted) been subject to regulation by the states. It contends that no change in law has occurred which justifies the Commission's claim of expanded jurisdiction. Moreover, it disagrees with the Commission's conclusion that the unbundled delivery by the previous public utility generation supplier directly to an end user is in interstate commerce. It argues that the FPA was never intended to disturb the jurisdiction of state regulators that existed prior to its passage and that retail transmission of electric energy by a public utility to an end user was under state jurisdiction before the Attleboro decision and has remained under state jurisdiction in the over sixty years following Attleboro. Even after unbundling, according to IL Com, transmission to a retail customer still involves a retail sale of transmission.

NARUC and VA Com assert that the legislative history provides little support for the Commission's conclusion that the act of unbundling generation from delivery serves to shift jurisdiction from a state commission to the Commission. If anything, they contend, the jurisdictional structure of the FPA is predicated on the distinction between retail and wholesale transactions, not bundled and unbundled services. They assert that the Commission should conclude that the rates, terms and conditions of service for delivery of power by a utility to an end-use customer are subject to the jurisdiction of the state commission regulating the utility, regardless of the identity of the party generating **[31,338]** or reselling the power or the facilities used to transport the power.

NARUC asserts that the Commission did not address a point raised in NARUC's reply comments as to how the removal of generation serves to unbundle the retail delivery function into separate transmission and distribution services. It maintains that the Commission simply assumes that a resulting transmission transaction is created when power is sold to a retail consumer by someone other than the utility delivering the power.[458]

MI & NH Coms ask the Commission to vacate those portions of the Rule that find that the Commission has jurisdiction over the transmission component of an unbundled retail sale in a local retail wheeling transaction. They assert that the Commission should confine its activity to wholesale transactions or those interstate transactions that do not implicate matters of local concern. They argue that the dual federal/state regulatory scheme establishes that Congress' intent is that state regulation of retail wheeling is not preempted by federal law as established in FPA section 201. They oppose unnecessary federal intrusion into local matters under a one-size-fits-all approach and assert that the retail wheeling initiatives in New Hampshire and Michigan are tailored to the unique utility environment in each state.

Central Illinois Light argues that unbundling of retail electric service does not change the states' longstanding jurisdiction over retail electric service and local distribution,

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[458] *See also* IA Com (use of a utility's transmission system to serve its own retail customers is a bundled part of the retail sale transaction, which supports a simpler jurisdictional test holding that a movement of power by the last utility in any chain of delivery to a retail customer is a distribution transaction).

even when that service involves the use of transmission in interstate commerce. It asserts that 201(b)(1) ("transmission of electric energy in interstate commerce") cannot be read in a vacuum.

MN DPS & MN Com and OH Com assert that the Commission should have no role in the regulation of retail services, be they bundled or unbundled. They argue that, in refusing to grant the Commission authority over retail wheeling, Congress left jurisdiction over retail electric service to the states. They conclude that the Final Rule contains insufficient legal and/or policy justification for the Commission's assertion of jurisdiction over unbundled retail transmission services.

MN DPS & MN Com assert: "FERC bases its usurpation of state authority over retail transmission rates on its claim that balkanization would occur without the assertion of FERC authority. Therefore, the parties are entitled to rehearing so that this essential issue can be further analyzed." (MN DPS & MN Com at pp. 1-3).

FL Com argues that the Commission has not justified why the act of unbundling prices expands the Commission's jurisdiction into retail marketing areas. It argues that Section 212(g) of the FPA has the effect of prohibiting the Commission from usurping existing state jurisdiction over retail transmission service, whether bundled or unbundled. According to FL Com, FERC's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. It supports wheeling in jurisdiction for state commissions and wheeling out and wheeling through jurisdiction for the Commission.

IN Com opposes federalization of retail wheeling transactions within a state's boundaries as contrary to the FPA's legislative history and case law.

NJ BPU asserts that by claiming jurisdiction over unbundled retail transmission, the Commission is creating a disincentive for states to implement retail access because, by ordering retail access, the states may be relinquishing their jurisdiction over unbundled retail transmission terms and conditions -- jurisdiction that they would maintain under a bundled scenario.[459] PA Com argues that the Commission does not have the authority to order retail wheeling and that the jurisdictional formula is challengeable on engineering and legal grounds. It concludes that the Commission does not have jurisdiction over unbundled interstate retail transmission service. PA Com notes that the 1996 House and Senate hearings have **[30,339]** raised the question whether the Commission has the statutory authority to restructure the electric industry. PA Com questions the Commission's definition of the "traditional tasks of state and federal regulators" on the basis of section 201(b) of the FPA, the Supremacy Clause, and the Tenth Amendment of the U.S. Constitution.

Support Broader Assertion of Jurisdiction by the Commission Over Retail Wheeling

NY Utilities declare that the Commission has jurisdiction over retail wheeling from the source to the load, but does not have jurisdiction over transmission in bundled

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[459] *See also* PA Com.

retail service. They assert that the Commission's reliance on state jurisdictional local distribution as a predicate to abstain from allowing retail wheeling stranded cost recovery is without foundation. They further assert that a unique element that sets local distribution apart from transmission is not the size of the facility or the length of travel, but that transportation is bundled with a retail sale. According to NY Utilities, the plain meaning of the FPA shows that local distribution is bundled retail service. They claim that the legislative history, to the extent necessary, and court cases support FERC jurisdiction over all aspects of retail wheeling, but makes clear that the Commission cannot regulate bundled retail service. They add that the NGA also demonstrates that local distribution means bundled retail service.

Commission Conclusion

In concluding that this Commission has exclusive jurisdiction over the rates, terms and conditions of unbundled retail transmission by public utilities in interstate commerce, the Commission in Order No. 888 thoroughly examined the statutory language of the FPA and its legislative history, and relevant FPA and NGA case law. While the state commissions on rehearing would like us to draw a bright line that gives them, to varying degrees, jurisdiction over retail interstate transmission by public utilities, no party on rehearing has raised any legislative history or case law that was not previously considered and that would support the proposition that states have jurisdiction over any unbundled transmission in interstate commerce. As explained below, we reaffirm our jurisdictional interpretation on rehearing and believe that it is

supported by the recent decision in *United Distribution Companies v. FERC.*[460]

Many of the rehearing arguments focus on the fact that states historically (even prior to the FPA) regulated retail transmission insofar as it was a component of bundled electric service to an end user, and they argue that by asserting jurisdiction over unbundled retail transmission, the Commission is somehow "taking away" jurisdiction the states previously had. The flaw in these arguments is their inherent assumption that jurisdiction over transmission service turns upon the question of whether the transmission service is being provided for "wholesale" or "retail" power sales. That is not the case. The question of jurisdiction rather turns upon the extent of the Commission's exclusive jurisdiction over transmission in interstate commerce under the FPA. The fact that states historically regulated most retail transmission service as a part of a bundled retail power sale is not the result of a legal requirement; it is the practical result of the way electricity has historically been bought and sold. However, the shape of power sales transactions is rapidly changing. Rather than claiming "new" jurisdiction, the Commission is applying the same statutory framework to a business environment in which, as discussed below, retail sales and transmission service are provided in separate transactions.

In the past, retails ales occurred almost exclusively on a bundled basis (i.e., the same entity provided a delivered

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[460]88 F.3d 1105, 1152-53 (1996) (*United Distribution Companies*).

product called electric energy and transmission was part and parcel of that product). The FPA clearly reserves the right to regulate retail sales of electric energy to the states. As we explained in the Final Rule, however, in today's markets, and increasingly in the future as more states adopt retail wheeling programs, retail transactions are being broken into products that are being sold separately: transmission and generation. Moreover, these products are being sold increasingly by two or more different entities. For example, a transaction may **[30,340]** involve transmission service from one or more transmission providers who move power from a distant generation supplier, over the interstate transmission grid, to an end user. Because these types of products and transactions were not prevalent in the past, the jurisdictional issue before us did not arise and, contrary to IL Com's argument, the Commission cannot be viewed as "disturbing" the jurisdiction of state regulators prior to and after the Attleboro case.[461]

As we also explained in the Final Rule, the legislative history of the FPA and the relevant case law similarly reflect the historical market structure in which electricity and transmission generally were bought on a bundled basis.[462] Today's unbundled world simply was not contemplated and the cases do not resolve dispositively this jurisdictional issue. The case law focuses primarily on the bright line between wholesale sales and retail sales of energy, and transmission in interstate as opposed to intrastate commerce. It does not

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[461] *Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927).

[462] The case law is addressed extensively in Appendix G to the Final Rule and will not be repeated here.

address unbundled retail interstate transmission.[463] We therefore have interpreted the case law in light of changed circumstances and have relied in the first instance on the plain wording of the statute. We find compelling that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce without qualification; unlike our jurisdiction over sales of electric energy, which section 201 specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

Since the time Order No. 888 issued, the D.C. Circuit has addressed a similar issue in interpreting section 1(b) of the NGA, the provision that parallels section 201(b) of the FPA. Under section 1(b), the Commission's jurisdiction does not apply "to the local distribution of natural gas or to the

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[463]On rehearing, several parties argue that at least one court case, *Wisconsin-Michigan Power Co. v. FPC*, 197 F.2d 472 (7th Cir. 1952), *cert. denied*, 345 U.S. 934 (1953) explicitly applied the wholesale/retail distinction to distinguish transmission and local distribution services. The Commission discussed this case in detail in Appendix C to the Final Rule, *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,974-75; *mimeo* at 22-25. As we stated there, the court's interpretation of the legislative history of the FPA was at odds with both the plain words of the statute as well as the language of the House Report on the FPA (H.R. Rep. No. 1318 at p. 27). It also did not mention the Senate Report on the FPA, which clearly recognized jurisdiction over all interstate transmission lines, whether or not a sale of energy is carried by those lines (S. Rep. No. 621 at p. 48). We therefore reject arguments that this single case is in any way dispositive of the issue before us.

facilities used for such distribution." Similarly, under section 201(b) of the FPA, the Commission shall not have jurisdiction, except as specifically provided, "over facilities used for the generation of electric energy or over facilities used in local distribution. . ." In responding to arguments regarding the scope of state authority over "local distribution" of natural gas, the court distinguished between bundled and unbundled sales:

> States have been -- and are still -- permitted to regulate LDCs' bundled sales of natural gas to end-users because those transactions include transportation over local mains and the retail sales of gas. In contrast, states have never regulated the terms and conditions of interstate pipeline transportation. When the gas sales element is severed -- i.e., unbundled -- from the transactions, FERC retains jurisdiction over the interstate transportation component." [*United Distribution Companies*, 88 F.3d at 1153 (footnote omitted) (emphasis in original).]

The court's reasoning is also applicable to and supports our jurisdictional determination in Order No. 888.

Several state commissions point to section 212(h) of the FPA and argue that Congress, in refusing to grant the Commission authority to order retail wheeling, left all jurisdiction over retail transmission to the states. We disagree. What Congress did in section 212(h) was to prohibit us from ordering transmission directly to an ultimate consumer. We readily recognize and respect this prohibition. However, the

ability to order retail **[31,341]** wheeling is a separate issue from whether we have jurisdiction over the rates, terms and conditions of retail wheeling in interstate commerce that is ordered by a state or that is provided voluntarily. Congress, in enacting section 212(h), did nothing to modify our jurisdiction under sections 201, 205 and 206 over the rates, terms and conditions of interstate transmission by public utilities.

Similarly, we reject FL Com's arguments that section 212(g) of the FPA prohibits the Commission from asserting any jurisdiction over unbundled retail transmission. Section 212(g) prohibits the Commission from issuing an order that is inconsistent with any state law that governs retail marketing areas of electric utilities. As we stated in the Final Rule, while our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. We also reject arguments by the FL Com that this Commission's jurisdiction over transmission terminates at the territorial boundary of each electric utility in Florida. This argument is flatly contrary to the longstanding interpretation of the FPA by the United States Supreme Court.[464]

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[464] *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964) (*Colton* case). IN Com makes a similar argument and opposes "federalization" of retail wheeling within a state's boundaries. We reject this argument on the same basis.

Commission's Seven Factor Test

IL Com argues that the Commission should withdraw its technical test. It contends that retail wheeling jurisdiction should follow function and that the function served by public utility facilities in providing retail service does not change upon the unbundling of service to retail customers. According to IL Com, Commission jurisdiction would extend to the service of delivering electric energy by a public utility to wholesale customers, regardless of the nature and extent of the public utility's facilities used to make that delivery. Similarly, it asserts, state jurisdiction would extend to the service of delivering electric energy by a public utility directly to retail customers, regardless of the nature and extent of the public utility's facilities used to make that delivery.

NARUC argues that the seven-factor test does not result in the bright line discussed in *FPC v. Southern California Edison Company*, 376 U.S. 205 (1964). The facility-by-facility categorization of utility systems on a company-specific basis, it asserts, is hardly consistent with the Court's decision to make case-by-case analysis unnecessary.

OH Com asserts that the seven factors provide no useful insight into the nature of local distribution service. It adds that reliance upon technical tests to determine local distribution lacks legal foundation. It further contends that the jurisdictional bright line established by Congress focuses upon the nature of the transaction, not the functional or technical characteristics of a particular wire, in determining whose jurisdictional authority attaches to a particular transaction and facilities. It concludes that the Commission should adopt the

Ohio-proposed retail marketing area "wheeling in" jurisdictional approach.

PA Com contends that the Commission's seven indicia are not acceptable measures of local distribution and challenges each factor.

NH & MI Coms declare that the criteria for distinguishing transmission facilities from local distribution facilities should not be limited to the seven given in the Rule, but should allow consideration of any other relevant criteria for separating local concerns from matters legitimately federal in nature.

NJ BPU argues that the engineering-driven definition does not resolve many of the hazy areas. To the extent that the seven factors do not reflect or cannot be reconciled with the particular circumstances, it contends that the states may be hamstrung in their ability to make **[30,342]** reasoned decisions that comport with Order No. 888.[465]

Similarly, NY Com argues that five of the seven factors (1, 2, 4, 6,and 7) are not accurate when applied to large metropolitan areas and remote rural areas. It asserts that local distribution facilities are not necessarily close to retail customers and the assumption that local distribution facilities

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[465] *See also* WI Com (criteria do not appropriately reflect the mixed nature of many facilities in systems that are closely integrated and the application of the criteria to the electric system in Wisconsin would supplant state jurisdiction over a large number of facilities whose primary functions are local reliability and retail service).

are primarily radial in character fails to account for network systems. It adds that reconsignment or transportation of power to different markets can and does occur at the local distribution level. It further adds that the presence of meters is not a discerning characteristic of where interstate transmission ends and local distribution begins; meters are frequently not part of the transmission/local distribution interface. Nor, according to NY Com, are local distribution systems necessarily of reduced voltage. Instead of the 7 criteria, NY Com argues that the Commission should adopt a functional measure of local distribution based on factors 3 and 5 (interstate transmission ends and local distribution begins where electricity flows into a comparatively restricted geographic area and does not flow back out of that area and the power is consumed in that area) and on the traditional classification of the facilities by the state regulatory body (or what the utility has traditionally classified as local distribution).

Commission Conclusion

Several parties on rehearing do not like the seven-factor technical test for local distribution facilities that was set forth in Order No. 888. That test takes into account both technical and functional characteristics of the transaction involved. The parties on rehearing propose instead a variety of bright line tests. For example, IL Com wants state jurisdiction to extend to the "service" of delivering electric energy to retail customers, which it would define to give it jurisdiction regardless of the nature and extent of the facilities used to make the delivery. OH Com proposes that the Commission adopt a retail marketing area "wheeling in"

jurisdictional approach which would give it jurisdiction over facilities within territorial boundaries.

In response, we do not interpret the FPA to permit us in effect to rewrite the statute to give states jurisdiction over interstate transmission services. Moreover, we reject arguments of OH Com that our seven-factor test lacks legal foundation, and arguments of NARUC that we are somehow bound to develop a bright line test. While Congress established a jurisdictional bright line between wholesale and retail sales of energy, there is no such bright line that we can divine with regard to transmission and local distribution facilities. The Supreme Court, in both Colton and CL&P,[466] has instructed us that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. The seven factors will permit us to undertake this fact-specific determination.

We acknowledge the concerns raised by several state commissions that the seven-factor test does not, as NJ BPU puts it, resolve many of the hazy areas, and that there may be other factors that should be taken into account in particular situations. The seven-factor test is intended to provide sufficient flexibility to take into account unique local characteristics and historical usage of facilities used to serve retail customers. We specifically stated in the Final Rule that we will consider jurisdictional recommendations by states that take into account other technical factors that states believe are appropriate in light of historical uses of particular facilities.

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[466] *See Colton*, 376 U.S. at 210 n.6; CL&P, 324 U.S. at 531-36.

Moreover, we will defer to facility classifications and/or cost allocations that are supported by state regulatory authorities. For example, in the ongoing California electric utility restructuring proceeding, the Commission deferred to the State PUC's recommendations regarding the split between state-jurisdictional local distribution facilities and Commission-**[30,343]** jurisdictional transmission facilities.[467]

Oppose transmission of public utility purchases for sale at retail

IL Com objects to the transmission unbundling requirement if it is intended to require public utilities to take transmission services under their own FERC tariffs for purchases of power intended for distribution by the public utility to retail customers. According to IL Com, a distinction must be made between the public utility's use of its transmission system in cases in which the public utility purchases wholesale power for sale for resale, and cases in which the public utility purchases wholesale power to serve native load retail customers. It argues that the Commission cannot legally regulate, or place conditions on, the manner in which a utility uses its transmission system to make sales of electric energy at retail. It contends that the Commission must exempt public utility power purchases for sale at retail from the unbundling requirement. It recommends that the Commission insert the words "for sale for resale" after the word "purchases" in section 35.28(c)(2) and after the word "purchase" in section 35.28(c)(2)(i).

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[467] *Pacific Gas and Electric Company, et al.*, 77 FERC ¶61,325 at p. 61,325 (1996).

Commission Conclusion

The Commission rejects arguments of IL Com that if unbundled retail wheeling occurs either voluntarily or as a result of a state retail program, we cannot require the utility to take service under its own transmission tariff for sales to retail customers. This requirement is a term and condition of unbundled retail interstate transmission service and, as explained above, therefore is within our exclusive jurisdiction. Additionally, this should not in any way infringe on state retail programs or service to retail customers. Rather, it ensures that non- discriminatory transmission services are provided to all potential retail power competitors.

Further, as stated previously in Section IV.C.1.b (Transmission Providers Taking Service Under Their Tariff), we clarify that a transmission provider does not have to "take service" under its own tariff for the transmission of power that is purchased on behalf of bundled retail customers.

Oppose buy-sell transaction analysis

PA Com asserts that there is a potential for jurisdictional conflict with respect to buy-sell transactions that is a direct consequence of the technical-functional test (which PA Com challenges).

IL Com argues that states have exclusive authority to regulate buy-sell arrangements as bundled retail sales. It further argues that the Commission cannot make a bundled retail sale into an unbundled retail sale simply by characterizing it as the functional equivalent of an unbundled retail sale; by re-characterizing them the Commission is

effectively ordering the unbundling of buy-sell arrangements. It asserts that buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction and that the Commission should withdraw its assertion of jurisdiction over the retail transmission component of unbundled retail sales.

VT DPS contends that the Commission's rationale is flawed: "FERC's analysis rests on the same very shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies." According to VT DPS, all retail transactions are subject to state jurisdiction and asks the Commission to clarify that the Commission defines buy-sell as it did in the NOPR, but also acknowledge that it has no jurisdiction over such arrangements.

IN Com asserts that in the absence of any record of abusive and undermining actions by states under the guise of buy-sell arrangements, there is not even a remedial justification to touch buy-sell transactions. It contends that a difference between the FPA and the NGA warrants different treatment -- the FPA exempts from FERC jurisdiction local distribution and transmission of electric energy in intrastate commerce. By redefining interstate transmission, IN Com claims that the Commission proposes to do away with the meaning history has accorded to a variety of transactions previously considered wholly intrastate in nature. According to IN Com, states should be allowed **[30,344]** to experiment with and allow different forms of buy-sell transactions as part of the evolving marketplace.

Commission Conclusion

Four parties (PA Com, IL Com, VT DPS and IN Com) have raised concerns regarding the Commission's determination that it has jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third party. The Commission reiterates that we will have to address these situations on a case-by-case basis. We disagree with IL Com that States have exclusive authority to regulate the interstate transmission component of buy-sell transactions. Similarly, we deny the VT DPS request that we acknowledge no jurisdiction over such arrangements. The fact remains that these arrangements could be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. We reserve our authorities to ensure that public utilities and their customers are not able to circumvent non-discriminatory transmission in interstate commerce. In response to VT DPS' contention that the Commission's analysis here rests on the same shaky ground as its similar claim of jurisdiction over buy-sell arrangements by local gas distribution companies, we note that the D.C. Circuit recently affirmed the Commission's assertion of jurisdiction over buy/sell arrangements under the Natural Gas Act.[468]

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[468] *United Distribution Companies*, 88 F.3d at 1154-57.

State jurisdiction over the service of delivering electric energy to end users

Rehearing Requests

IL Com states that it is far from clear what FERC contemplates by the "service" of delivery of electric energy by a delivering utility in the retail wheeling transaction. It is equally unclear to IL Com whether the "service" to which Order No. 888 refers is a public utility activity over which state regulators would have jurisdiction. IL Com argues that it is the Illinois legislature, not FERC, that determines whether IL Com can regulate something called "delivery service."[469]

MO/KS Coms ask the Commission to clarify the meaning of the statement that even when the test for local distribution facilities identifies no local distribution facilities, the Commission believes that states have authority over the service of delivering electric energy to end users. According to MO/KS Coms:

> The authority to shop at retail and to sell at retail do not exist in the FPA. If the Commission's goal is to recognize the States' authority to establish conditions on retail competition, it need only acknowledge the

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[469] *See also* AK Com (should not create a fictional concept of delivery service -- the legal reality is that, under retail competition, state law will establish a customer's right to be served and a generation owner's right to produce power. AK Com asserts that the state can then attach conditions to those rights).

> State jurisdiction to establish the opportunity to shop and sell at retail. If this is what the Commission is seeking to accomplish by its discussion of 'delivery service,' then we support the Commission."[470]

Coalition for Economic Competition asserts that the Commission failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, and that the local regulatory commission may have no jurisdiction over either the sale or the transmission of the energy.

Commission Conclusion

Several parties ask us to clarify our conclusion that even when the seven-factor test for local distribution facilities does not identify local distribution facilities, we believe states have authority over the "service" of delivering electric energy to end users. We clarify that states have the authority to determine the retail marketing areas of electric utilities within their jurisdictions, and the end user services that those utilities must provide, but we did not in Order No. 888 intend to opine on the extent of authority given by state legislatures to their state commissions. Rather, our statement regarding state authority over the "service" of delivering electric energy is intended to recognize the historical and local nature of delivering power to end users and the **[30,345]** states' legitimate concerns and responsibilities in regulating local matters.

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[470]MO/KS Coms at pp. 1-13.

Deference to states

Rehearing Requests

Support broader deference

NARUC and IL Com argue that the Commission should not simply defer to state recommendations concerning the application of the seven-factor test or the recovery of stranded costs, but should conclusively rely on the findings by state commissions.

NY Com argues that the Commission should not limit deference to instances in which states order retail wheeling, but should defer to all state commission recommendations regarding the definition of local distribution facilities.

FL Com asserts that the Rule fails to say where deference will be given. It argues that the Rule should state that when a state commission has held a proceeding on matters related to the requirements of the Rule, the Commission shall give deference to the state commission decisions. Moreover, it asserts that the Commission should codify the deference standard: "When a state commission has held a proceeding on matters related to the requirements of this rule, the Commission shall give deference to the state commission decisions." (FL Com at pp. 7-9).

The commitment to defer to a state regulatory commission or agency, argues NE Public Power District, should be clarified with respect to utilities located in Nebraska, which has no such commission or agency. NE Public Power District assumes that deference will be accorded

to decisions of NE Public Power District's Board of Directors; if not, it asks the Commission to clarify.

PA Com asks the Commission to clarify what a state regulatory agency must demonstrate to secure deference and to define the term "consult." PA Com states that, in discussing the seven indicia, the Commission states that it will "consider" jurisdictional recommendations by states, which PA Com asserts is much different from deference. It also asserts that the Commission must clarify what it will do if a utility's classifications and/or cost allocations are not supported by state regulatory authorities.

Oppose deference to state authorities

TANC argues that the Commission erred in deferring to state regulatory authorities in drawing jurisdictional lines for local distribution facility classifications and/or cost allocations. According to TANC, the Commission unlawfully and unnecessarily abdicated its jurisdiction under the FPA (citing *New England Power Co. v. New Hampshire*, 455 U.S. 331, and *Nantahala Power and Light Co. v. Thornburg*, 476 U.S. 953). With respect to ISOs, it asserts that the Commission should not defer to state authority in making determinations with respect to classifications of facilities.

Commission Conclusion

In response to NARUC and IL Com's arguments that this Commission should not simply defer to state commissions regarding application of the seven-factor test but instead should conclusively rely on the findings of state commissions, we believe this is inconsistent with the case law which states

that local distribution it is a matter of fact for the Commission to determine as an original matter.[471] Additionally, we have an independent obligation to ensure that we are fulfilling our responsibilities under the FPA to regulate facilities that are used in interstate commerce. We cannot delegate our jurisdiction. However, we intend to provide broad deference to states in determining what facilities are Commission-jurisdictional transmission facilities and what facilities are state-jurisdictional local distribution facilities, so long as our comparability principles are not compromised and we are able to fulfill our responsibilities under the statute.

We reject FL Com's suggestion that we codify the deference standard. This is neither necessary nor appropriate. In response to NE Public Power District's request that we clarify to whom we would give deference in Nebraska, we clarify that because Nebraska does not have an electric regulatory commission or agency, there is no appropriate regulatory entity to whom our deference standard would apply; accordingly, we will address the **[30,346]** transmission/local distribution issue for Nebraska without giving deference to any particular entity. In response to PA Com's request that we clarify what we will do if a utility's classifications and/or cost allocation proposals are not supported by state regulatory authorities, we will make a determination based on the factual record before us in a particular case, taking into account the views of the state regulatory authority.

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[471] *See Colton and Connecticut Light and Power, supra.*

TANC has argued that we have unlawfully abdicated our jurisdiction by deferring to state recommendations. TANC confuses delegation of jurisdiction, which we cannot do, with willingness to defer to states based on their application of criteria that we have provided. Even in the cases in which the Commission defers to states' views, we will still independently evaluate all material issues and proceed only where substantial evidence supports the states' views. The Commission clearly can entertain requests for deference in these circumstances.

J. *Stranded Costs*

As indicated in our prior discussion in Section IV.A.5, there are two major overlapping transition issues that arise as a result of this rulemaking: stranded cost recovery and how to deal with contracts entered into under the prior regulatory regime. We here address stranded cost recovery and, as in the prior discussion, we believe it is important to explain the general context in which our stranded cost determinations have been made before addressing the various rehearing requests on this issue.

In Order No. 888, the Commission removed the single largest barrier to the development of competitive wholesale power markets by requiring non-discriminatory open access transmission as a remedy for undue discrimination. This action carries with it the regulatory public interest responsibility to address the difficult transition issues that arise in moving from a monopoly, cost-based electric utility industry to an industry that is driven by competition among wholesale power suppliers and increasing reliance on market-based generation rates. The most critical transition issue that

arises as a result of the Commission's actions in this rulemaking is how to deal with the uneconomic sunk costs that utilities prudently incurred under an industry regime that rested on a regulatory framework and a set of expectations that are being fundamentally altered.

The Commission determined in Order No. 888 that it must address stranded costs, and that it must do so at an early stage -- particularly in light of the lessons learned from our experience with similar issues in the natural gas area. We noted that when we did a similar restructuring in the gas industry, the D.C. Circuit invalidated the Commission's efforts precisely because the Commission had failed to deal with the stranded cost problem in a satisfactory manner.[472] We explained that, based on the lesson of AGD, the Commission cannot change the rules of the game without providing a mechanism for recovery of the costs caused by such regulatory-mandated change.

Since the time Order No. 888 issued, we have been provided with additional guidance from the court in the natural gas area, which has further helped to inform our decisions here. In its decision on review of Order No. 636,[473] the D.C. Circuit upheld the Commission's decision to allow the recovery of gas supply realignment costs. In so doing, the court, while questioning a specific feature of the stranded cost recovery mechanism employed in Order No. 636, has

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[472] *Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) (*AGD*).

[473] *United Distribution Companies v. FERC*, 88 F.3d 1105 (1996) (*United Distribution Companies*).

nevertheless again reaffirmed the basic principle that stranded cost recovery is an appropriate component of a regulatory policy aimed at accomplishing a fair and reasonable transition to competitive markets. The question as to the Commission's ability to allow the recovery of stranded costs has been laid to rest.

The task before the Commission in this rulemaking is thus to determine how best to meet its responsibility to address the costs of the transition to a competitive industry, particularly insofar as those costs are stranded, or in effect rendered unrecoverable, as a result of the transmission access required by us under the **[30,347]** FPA.[474] As the rehearing arguments demonstrate, there is no consensus on how the Commission should address the stranded cost issue. In fact, petitioners are at polar extremes as to what the Commission should do regarding stranded costs. Some argue that the Commission has gone too far in permitting utilities to seek recovery of stranded costs, whether such costs are associated with wholesale requirements contracts, with retail-turned-wholesale customers, or with retail customers that obtain retail wheeling.[475] Others argue that the Commission has not

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[474]Such access may be the open access required under this Rule or case-by-case transmission access ordered pursuant to FPA section 211.

[475]We note that the regulations implementing this Rule use "wholesale stranded cost" and "retail stranded cost" as shorthand terms to refer to the different situations in which a utility may experience stranded costs. However, as the definitions of those terms make clear, it is not the nature of the costs (wholesale vs. retail) that is controlling for purposes of stranded cost recovery

gone far enough and that it must broaden the scope of stranded cost recovery permitted under the Rule. Indeed, some would have us be the guarantor for recovery of all uneconomic costs that might be stranded in the move to more competitive markets, no matter how tenuous the nexus to this Rule, and irrespective of state-Federal jurisdictional complexities. Some support the Commission's decision to recover stranded costs directly from the departing customers. Others would prefer that the Commission require utilities to absorb a portion of their stranded costs or that the Commission spread the burden of stranded costs among all of the utility's customers. Some object that the Commission's approach to stranded costs in the electric industry is different from that adopted in the gas industry. Some entities support the Commission's revenues lost approach for measuring a departing customer's stranded cost obligation. Others propose different methods for computing stranded costs.

Given the plethora of positions that entities have raised both initially and on rehearing concerning stranded costs, the Commission has taken a careful, measured approach with regard to stranded cost recovery. The Commission has balanced a number of important interests in order to achieve what it believes will be a fair and orderly transition to

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under this Rule. Rather, the controlling factors are the status of the customer (wholesale transmission services customer vs. retail transmission services customer) with whom the costs are associated, and whether the transmission tariffs used by the customer to escape its former power supplier (thus causing the stranding of costs to occur) were required by this Commission or by a state commission. As a result, "retail stranded costs" refers to stranded costs associated with retail wheeling customers.

competitive markets. These interests include the financial stability of the electric utility industry, upholding the regulatory bargain under which utilities made major capital investments, and not shifting costs to customers that had no responsibility for causing those costs to be incurred. The Commission also has adopted an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

The balancing of interests and considerations described above is reflected in the following central components of the Rule's stranded cost provisions, which are reaffirmed herein.[476] First, the Commission has determined that the most reasonable, legally supportable approach is one that permits utilities to seek recovery of wholesale stranded costs under this Rule (whether the stranded costs are associated with a departing wholesale requirements customer or with a retail-turned-wholesale customer) only in those cases in which there is a *direct nexus* between the availability and use of Commission-required transmission access[477] and the **[30,348]**

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[476]We reaffirm below our basic determinations, but make certain clarifications on limited issues and grant rehearing on the municipal annexation issue.

[477]As we explain below, by "Commission-required transmission access" we mean the open access transmission required under this Rule or required pursuant to a section 211

stranding of costs. In order for the utility to be eligible to seek recovery of stranded costs from a departing customer, the customer must have obtained access to a new generation supplier through the use of the former supplying utility's Commission-required transmission tariff (i.e., its open access tariff or a tariff ordered pursuant to FPA section 211), not through the use of another utility's transmission system.

Other cost recovery issues are more appropriately addressed outside the context of this Rule. For example, the Rule is not intended to apply to costs associated with the normal risks of competition, such as self-generation, cogeneration, or loss of load, that do not arise from the new, accelerated availability of Commission-required transmission access. If a customer leaves its utility supplier by exercising options that could have been undertaken prior to mandatory transmission under Order No. 888 or the Energy Policy Act, or that do not rely on access to the former seller's transmission, there is no direct nexus to Commission-required transmission access and thus no opportunity for stranded cost recovery under the Rule.

Second, the Commission has limited the opportunity to seek stranded cost recovery under the Rule primarily to two discrete situations: (1) costs associated with customers under wholesale requirements contracts executed on or before July 11, 1994 (referred to in the Rule as "existing wholesale

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order, as well as transmission provided prior to Order No. 888 (and not pursuant to a section 211 order) where such transmission was provided on a case-by-case basis to comply with the Commission's comparability requirement. *See* note 484 *infra*.

requirements contracts") that do not contain an exit fee or other explicit stranded cost provision; and (2) costs associated with retail-turned-wholesale customers. With regard to the existing wholesale requirements contracts, the Commission also has made a finding that it is in the public interest to permit amendments to add stranded cost provisions to these contracts, even if they contain *Mobile-Sierra* clauses, if case-by-case evidentiary burdens are met. We do not interpret the *Mobile-Sierra* public interest standard as practically insurmountable in extraordinary situations such as this one where historic statutory and regulatory changes have converged to fundamentally change the obligations of utilities and the markets in which they and their customers will operate.

Third, Order No. 888 *does not guarantee* that a utility will be allowed to recover stranded costs. Rather, it provides an opportunity for such recovery. To be eligible to recover stranded costs from a departing customer in a particular case, the utility must demonstrate that it incurred costs to provide service to the customer based on a reasonable expectation of continuing service to that customer beyond the contract term.[478] In the case of stranded costs associated with wholesale requirements contracts customers, if the contract contains a notice of termination provision, that provision is strong evidence that the parties were aware that at some point in the future the customer might seek to find another supplier.

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[478]We have made a minor revision to the regulatory text, section 35.26(c)(2), to conform the language of that section with sections 35.26(b)(1) and (5). A conforming revision has been made to section 35.26(d)(2)(i).

Therefore, there is a rebuttable presumption of no reasonable expectation, and therefore no opportunity for stranded cost recovery unless the utility can overcome the presumption.

The Commission has concluded that direct assignment of stranded costs to the departing customer (through either an exit fee or a surcharge on transmission) is the appropriate method for recovery of stranded costs under the Rule. In reaching this conclusion, the Commission carefully weighed the arguments supporting direct assignment of stranded costs against those supporting a more broad-based approach, such as spreading stranded costs to all transmission users of a utility's system, and also took into account the fact that we applied a different approach in the natural gas area. The central considerations that support a direct assignment approach in the electric industry are that the approach follows the traditional regulatory concept of cost causation, it avoids shifting costs to customers that had no responsibility for causing them to be incurred or for causing them to be stranded, and it is still possible to apply such an approach at this stage of the industry's evolution.

[30,349]

There is no question that, without the stranded cost recovery mechanism, some customers would be far more likely to switch to lower-cost suppliers and enjoy sooner the benefits of a competitive power market. But, as detailed in Order No. 888, such an approach may result in higher costs for other customers. We thus have had to balance the potential for earlier benefits for some customers against other public interest considerations, most particularly the need to provide a fair mechanism by which utilities can recover the costs of past investments under traditional regulatory concepts of

prudently incurred costs and cost causation. The result is not to deny competitive advantages, but only to delay their full realization for some customers so that all customers ultimately will benefit.

While Order No. 888's cost causation approach is different from the Order No. 636 cost spreading approach that was affirmed in the *United Distribution Companies* case, we believe it is the preferable approach given the early stage of the electric utility's competitive transition. We do not read the court's opinion as precluding the Commission from adopting a direct assignment approach in Order No. 888, particularly where, as here, the Commission has fully explained and justified the reasons for following traditional cost causation principles. In addition, although the *United Distribution Companies* court remanded for further consideration (in light of Order No. 636's cost spreading approach) the decision not to require any pipeline absorption of gas supply realignment costs, the Commission has fully explained how its decision in Order No. 888 not to require any utility absorption of stranded costs is consistent with its decision to follow traditional cost causation principles. With respect to the fundamental conclusion that utilities should be permitted an opportunity to recover their prudently incurred costs, Order No. 888 is fully consistent with Order No. 636. Although the Commission in Order No. 888 chose a direct assignment method (rather than the cost-spreading approach in Order No. 636) for purposes of allocating stranded cost responsibility among customers, the approach used by the Commission in Order No. 888 is not governed by decisions in Order No. 636, but in either event the Commission must demonstrate that its choice of methods is based on reasoned decision-making.

In considering the stranded cost issues that may arise in the transition to competitive markets, the Commission also has taken cognizance of significant changes involving retail customers and the stranded cost issues that arise as retail customers convert to wholesale customer status (*e.g.*, through municipalizations) in order to obtain the open access afforded by Order No. 888, or as they obtain retail wheeling required by state commissions. These situations involve new and complex jurisdictional issues and represent the bulk of potential stranded costs facing the industry. We believe it is important to clarify the Commission's decisions as to when it will entertain requests for stranded cost recovery in these situations, and our reasons for doing so.

The Commission's determination that it, rather than the states, should be the primary forum for addressing stranded costs associated with a retail-turned-wholesale customer[479] is limited to those cases in which there is a *direct*

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[479]In Order No. 888 and here, we sometimes use the shorthand expression "retail-turned-wholesale" customer. By this we do not mean that a retail customer who is an ultimate consumer ceases to be an ultimate consumer, or that this customer begins to purchase electric energy for resale. Rather, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility system, a newly- created entity becomes a wholesale power purchaser on behalf of retail customers who were formerly bundled customers of the historical local utility power supplier. The new municipal utility is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-

nexus between the availability and use of Commission-required transmission access and the stranding of costs. We believe we have both the authority and the obligation to provide an opportunity stranded cost recovery in these situations because the bundled retail customer would not be able **[30,350]** to obtain access to the new supplier *but for* the Commission's order requiring transmission. The creation of a new wholesale entity to purchase power on behalf of retail customers would not, by itself, trigger stranded costs. IN the absence of transmission access from the historical supplier of the retail customers, the new entity would have to remain on the historical supplier's generation system because it would have no way to reach other power suppliers and stranded costs would not occur.[480] Therefore, there is a causal nexus between the stranded costs and the availability and use of the tariff services *required by the Commission*.[481] Moreover, because of

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wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

[480]Exceptions would be self-generation or construction by the new entity of its own transmission line, in which case, as noted earlier, the stranded cost provisions of Order No. 888 would not apply because such options have always been available as alternatives to purchasing power from the historical supplying utility and do not involve the use of the utility's transmission facilities under an open-access tariff. Thus the departure of customers under these circumstances cannot be linked to the open-access requirements of this Rule.

[481]As discussed in greater detail in sections IV.J.6 and IV.J12 below, we clarify that the opportunity for recovery of stranded costs in a retail-turned-wholesale situation is limited to

this causal nexus between the use of a jurisdictional utility's Commission-required transmission tariff and the potential for foregone revenues by that jurisdictional utility as a result of the Commission-required access, the stranded costs associated with a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In contrast, in the situation in which a bundled retail customer obtains retail wheeling, stranded costs are directly caused by the availability and use of unbundled retail services *required by the state commission*, not this Commission.[482] Thus, the Commission believes that states, not the Commission, should be the primary forum for costs associated with a bundled retail customer that obtains retail wheeling. The Commission's decision to entertain requests to recover stranded costs caused by retail wheeling in *only* a limited circumstance (where the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on a policy decision

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cases in which the former bundled retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of its former supplier. We have revised section 35.26(b)(1)(i) of the Commission's regulations accordingly.

[482]Unbundled retail transmission services required by a state commission could be taken under the same *pro forma* open-access tariff sued by wholesale customers or, if determined appropriate by the Commission, under a separate retail tariff filed at the Commission. The critical point, however, is that in either case, the unbundled services are required by the state and not by this Commission.

by the Commission that it will step in to fill a regulatory "gap" that could result in no effective forum in which utilities would have an opportunity to seek recovery of prudently incurred costs.

Finally, after considering various proposals regarding how stranded costs should be calculated, and reviewing the arguments of petitioners on rehearing, the Commission continues to believe that the revenues lost approach is the fairest and most efficient way to determine the amount of stranded cost assigned to a departing customer during the transition to a competitive wholesale bulk power market. The Commission has rejected an asset-by-asset approach as overly complicated and costly.

We respond below to the specific arguments raised on rehearing and elaborate on the above determinations.

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[pp. 30,402-30,424]

[30,402]

6. Recovery of Stranded Costs Caused by Retail- Turned-Wholesale Customers

In Order No. 888, we concluded that this Commission should be the primary forum for addressing the recovery of stranded costs caused by a retail-turned-wholesale customer.[672]

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[672] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,818-19; *mimeo*

We stated that if such a customer is able to reach a new generation supplier because of the new open access (through the use of a FERC-filed open access transmission tariff or through transmission services ordered pursuant to section 211 of the FPA), any costs stranded as a result of this wholesale transmission access should be viewed as "wholesale stranded costs." We explained that there is a clear nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs and that, in these circumstances, this Commission should be the primary forum for addressing recovery of such costs.[673]

We said we will not be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory. We indicated that in these situations there is no direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of prudently incurred costs. The risk of an existing municipal utility expanding its territory was a risk prior to the Energy Policy Act and prior to any open access requirement.

Nevertheless, we did express concern that there may be circumstances in which customers and/or utilities could

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at pp. 534-37.

[673]We indicated that we will require the same evidentiary demonstration for recovery of stranded costs from a retail-turned-wholesale customer (and will apply the same procedures for determining stranded cost obligation) as that required in the case of a wholesale requirements customer.

attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission -- either this Commission or state commissions -- to address recovery of stranded costs. We reserved the right to address such situations on a case-by-case basis.

Rehearing Requests Opposing Retail-Turned-Wholesale Jurisdiction

A number of entities challenge the Commission's assertion that costs associated with retail-turned-wholesale customers would not be stranded but for the FERC-jurisdictional transmission access requirement. They assert that the condition precedent to municipalization is the operation of a state process, and thus that it cannot be the case that the recovery of costs caused by a retail-turned-wholesale customer is "not subject to regulation by the States." They submit that such costs would not be stranded but for the action of state legislators or state regulators in granting authority for the customer's status change. They argue that any nexus that the Commission's authority under the FPA has to wholesale transmission services subsequently provided to the new **[30,403]** wholesale customer is entirely derivative of the state's action.[674]

A number of entities argue that jurisdiction over costs that are stranded when a retail customer becomes a wholesale customer should be left to the states because the facilities used to provide retail service to these retail customers were subject

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[674] *E.g.*, NARUC, TAPS, Nucor, Suffolk County, IL Com, Multiple Intervenors, APPA, CAMU, WI Com, NASUCA.

to state jurisdiction and were included in retail rate base when the service was rendered.[675] They argue that because the Commission had no jurisdiction over the public utility facilities and costs incurred to serve retail-turned-wholesale customers, it has no jurisdiction to address those public utility costs if they become stranded. Thus, according to these entities, the conversion of the customer from retail to wholesale does not simultaneously effectuate a conversion of the costs from retail to wholesale.

AR Com and MO/KS Coms submit that jurisdiction over the costs incurred for historical retail customers does not shift unless the parties themselves make those costs a part of their new wholesale contract. NY Com submits that the Commission should recognize the states' jurisdiction to set the level of stranded costs associated with retail-turned-wholesale customers to be recovered in wholesale transmission rates set by FERC. FL Com asserts that state authorities are in a better position to assess the extent of stranded facilities and their costs, and that the Commission's involvement should be limited to that requested by a state by petition.

OH Com states that the Commission's position on stranded costs associated with retail-turned-wholesale customers invites second-guessing of state commission determinations and encourages forum shopping by introducing more than one stranded cost treatment within a single state jurisdiction. It expresses concern that utilities may seek to

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[675] *E.g.*, ELCON, IL Com, IN Com, American Forest & Paper, AR Com, MO/KS Coms, NJ BPU, Suffolk County, WY Com, VA Com, FL Com, NARUC, TAPS.

creatively disaggregate into generation, transmission, and distribution companies in ways to deliberately recast traditional retail relationships as wholesale in an effort to obtain favorable regulatory treatment of stranded costs.

IN Com submits that Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers will discourage state legislatures from making municipalization more available. VT DPS and Valero argue that the threat of a stranded cost surcharge will erect a new barrier to the formation of municipal utilities. They note that the Rule refers to one commenter's observation that, if *Otter Tail* could have made a stranded cost claim against the municipal utility that Elbow Lake planned to create, *Otter Tail* would not have needed to refuse to wheel and there would never have been an *Otter Tail* case. They submit that the Commission never addressed whether, or why, it believed the point to be wrong.

VT DPS and Valero also assert that the Rule represents a major inconsistency with prior Commission treatment of municipalization. They submit that the Commission historically promoted franchise competition between municipalities and utilities by holding tariff provisions that restrict such competition to be anticompetitive and unreasonable.[676]

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[676]VT DPS and Valero cite in this regard *Florida Power & Light Company*, 8 FERC ¶61,121 (1979); *Power Authority of the State of New York v. FERC*, 743 F.2d 93 (2d Cir. 1984); *Metropolitan Transportation Authority v. FERC*, 796 F.2d 584 (2d Cir. 1986).

American Forest & Paper submits that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's actions in the natural gas industry, where the Commission has encouraged competition at the retail level through competitive bypass and has not created barriers to competitive entry by imposing transition charges or exit fees on converting customers.[677]

Nucor objects that the Rule does not address the substantive findings, the common sense rationale, or the jurisdictional distinction drawn in *United Illuminating*.**[30,404]**[678] It contends that the Commission's observation in Order No. 888 that there may not be a state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers and hence that the Commission should be the primary forum for addressing such stranded costs is flawed because there always is a state forum to address such cost recovery (the adequacy of the relief provided is a very distinct issue) and open access transmission does not and cannot cause retail competition to occur.[679]

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[677] American Forest & Paper cites in support of its position Great Lakes Gas Transmission Limited Partnership, 68 FERC ¶61,376 (1994).

[678] *United Illuminating Company*, 63 FERC ¶61,212, *reh'g denied*, 64 FERC ¶61,087 (1993) (*United Illuminating*).

[679] *See also* Suffolk County Rehearing (Commission's analysis in *United Illuminating* was correct; nothing has changed to warrant the Commission's rejection of that analysis).

Commission Conclusion

We will reject the requests for rehearing of our decision to be the primary forum for addressing the recovery of stranded costs caused by retail-turned-wholesale customers. We find the requests for rehearing on this issue unpersuasive. While it may be the case, as some entities suggest, that state action is a condition precedent to municipalization, the rehearing petitions ignore the fact that the Rule covers situations in which open access is also a condition precedent to the municipalized customers leaving their existing supplier's system. Order No. 888 does not propose that the Commission be the primary forum for stranded cost recovery for all cases of municipalization. Instead, our holding is limited to those cases in which the new wholesale entity uses Commission-mandated transmission access to obtain new power supply on behalf of retail customers that were formerly supplied power by the utility providing the transmission service.[680]

As we explained in Order No. 888, in such cases there is a direct nexus between the FERC-jurisdictional transmission access requirement and the exposure to non-recovery of costs stranded as a result of this wholesale transmission access. Thus, the stranded costs associated with

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[680]In the case of municipalization, the bundled retail customers of a local utility become the bundled retail customers of the new municipal utility. As explained above, we call this a "retail-turned-wholesale customer" situation because the new municipal entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply.

retail-turned-wholesale customers for which Order No. 888 provides an opportunity for recovery would not have been incurred but for the action of this Commission in requiring a utility to make unbundled transmission services available. In these cases, the former bundled retail customers of the historical supplying utility (now the bundled retail customers of the new municipal system) would not have obtained access to new power supply but for the Commission's order mandating transmission. Without the regulatory mandate to provide access, the utility would have indirectly continued sales to the same retail customers because the new municipal utility purchasing power on the retail customers' behalf would have had no way to reach other power suppliers. In this situation, there would be no stranded generation costs. In other words, the creation of a municipal utility intermediary to purchase power at wholesale would not, by itself, trigger stranded costs. Rather, it is the access from the historical supplier of the bundled retail customers that is the condition precedent to reaching other power suppliers and thereby triggering stranded costs. Therefore, there is a clear causal nexus between the stranded costs and the availability and use of the tariff required by the Commission.

Costs that are exposed to nonrecovery when a retail customer or a newly-created wholesale power sales customer ceases to purchase power from the utility and does not use the utility's transmission system to reach a new generation supplier (*e.g.*, through self-generation or use of another utility's transmission system) do not meet the definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of the new open access.

In response to the argument that conversion of a customer from retail to wholesale would not simultaneously effectuate a conversion of the costs from retail to wholesale, we believe this argument confuses **[30,405]** the issue. We note that we have defined stranded costs as wholesale or retail on the basis of whether wholesale or retail open access is the cause of the costs being stranded, not on the basis of the original retail or wholesale characteristic of the costs. Thus, even though costs may have been originally incurred as retail-related costs, the precipitating event that results in such costs being stranded in the retail-turned-wholesale customer scenario is the use by the new wholesale customer of the Commission-mandated tariff. When a customer is able to use the Commission-required tariff to reach another generation supplier, it causes the utility to incur an economic cost in providing transmission service that is equal to the foregone revenues that the utility reasonably expected to receive under a state regulatory regime. Thus, because of the causal nexus between the use of a former supplying utility's Commission-mandated transmission tariff and the potential for foregone revenues by that utility as a result of the Commission-required access, the costs stranded by a retail-turned-wholesale customer are properly viewed as economic costs that are jurisdictional to this Commission.

In response to those entities that express concern that the Commission's position on stranded costs associated with retail- turned-wholesale customers invites second-guessing of state commission determinations, we emphasize that we have assumed primary authority to address such costs only in a limited category of cases where there is a direct nexus between the availability of Commission-required open access and the stranding of costs when the former customer uses the

former supplying utility's transmission system (through its open access tariff or a section 211 order) to reach a new supplier. We indicated in Order No. 888 that if the state has permitted any recovery from departing retail-turned-wholesale customers, such amount will not be stranded for purposes of this Rule. We will deduct that amount from the costs for which the utility will be allowed to seek recovery under this Rule from the Commission. In so doing, however, we are not second-guessing the states as to what a utility may recover under state law. Additionally, we will give great weight in our proceedings to a state's view of what might be recoverable.

We also reject the argument that the Commission's position on stranded costs associated with retail-turned-wholesale customers encourages forum shopping. To the contrary, as we said in Order No. 888, to avoid forum shopping and duplicative litigation of the issue, we expect parties to raise claims before this Commission in the first instance. We believe that this Commission should be the primary forum because, without the open access provided by the Rule, the new municipal utility would not be able to reach a new supplier and, as a result, would not cause the utility to incur stranded costs (as defined in this Rule).

We reject as misplaced arguments that the Rule represents a major inconsistency with the Commission's historical promotion of franchise competition between municipalities and utilities and that it will discourage municipalization.[681] It continues to be the Commission's

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[681] In response to VT DPS and Valero, we note that whether or not Otter Tail may have agreed to wheel power for the municipal

policy to encourage competition. Indeed, the goal of Order No. 888 is to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers. However, the purpose of the stranded cost policy is neither to encourage nor to discourage municipalization, but rather to facilitate a fair transition to competition and to ensure stability in the industry during that transition. As we discuss elsewhere in order, we believe that this Commission must address the recovery of the costs of moving from a monopoly-regulated regime **[30,406]** to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced. On this basis, we believe that if a new wholesale entity such as a municipal utility uses Commission-required open access to reach a new supplier on behalf of its retail customers (previously retail customers of the former supplier), the former supplying utility should be given an opportunity to recover legitimate, prudent and verifiable costs that it incurred under the prior regulatory regime to serve that customer.

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utility that Elbow Lake planned to create if Otter Tail could have made a stranded cost claim against that municipal utility is of no moment to the Commission's decision in Order No. 888 to allow utilities the opportunity to seek recovery of stranded costs associated with retail- turned-wholesale customers. The Court in *Otter Tail* did not address the stranded cost issue because it was not presented in that case. Nor was the Court presented with the extraordinary circumstances -- the historic statutory and regulatory changes, including the requirement of open access, that have converged to fundamentally change the obligations of utilities and the markets in which they operate -- that have justified this Commission's Order No. 888 stranded cost policy.

In response to American Forest & Paper's argument that recovery of 100 percent of stranded costs caused by municipalization is inconsistent with the Commission's policy in the natural gas industry of allowing competitive bypass without imposing transition charges or exit fees on converting customers, we note that industrial gas customers who bypass a local distribution company's (LDC) facilities do not escape transition costs quite so easily as suggested by American Forest & Paper. It is true that, when the end user bypasses the LDC to reach an interstate pipeline different from the pipeline serving the LDC, the Commission views the bypass as a risk of competition from which the LDC should not be shielded.[682] However, when the end user bypasses the LDC to reach the same interstate pipeline that serves the LDC, the Commission may take certain actions to minimize adverse effects on the LDC and its remaining customers.[683] Moreover, an end user that bypasses an LDC to reach the same pipeline that serves the LDC would, in any event, be allocated a share of the pipeline's gas supply realignment costs (if any), since those costs are allocated based on current contract demand (or usage).[684] Accordingly, we see no inconsistency between our

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[682]Texas Gas Transmission Corporation, 65 FERC ¶61,275 (1993).

[683]*Texas Gas Transmission Corporation*, 69 FERC ¶61,245, *reh'g*, 70 FERC ¶61,207 (1995) (requiring pipeline to offer LDC a reduction in its contract demand).

[684]*See Southern Natural Gas Company*, 75 FERC ¶61,046 at p. 61,158 (1996); *Arcadian Corporation v. Southern Natural Gas Company*, 67 FERC ¶61,176 at p. 61,538 (1994). *See also United Distribution Companies*, 88 F.3d at 1181. As the *United*

bypass policy for the natural gas industry and Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers. Similar to our refusal to shield LDCs from the adverse effects of an end user's bypass to reach a different pipeline than serves the LDC, Order No. 888 does not provide an opportunity for stranded cost recovery where a retail-turned-wholesale customer uses another utility's transmission system to reach a new supplier. As we note above, the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers is limited to those cases in which the former retail customer obtains (either directly or through another wholesale transmission purchaser) unbundled transmission services from its former supplying utility. In the case of an end use customer bypassing the LDC to reach the same pipeline that serves the LDC, the end use customer would similarly be allocated a share of the pipeline's gas supply realignment costs. As a result, American Forest & Paper's attempt to rely on the Commission's gas bypass policy is misplaced.

We also disagree with those entities that argue that the Commission has failed to adequately distinguish Order No. 888's treatment of stranded costs associated with retail-turned-wholesale customers with the Commission's decision in *United Illuminating*. As we stated in Order No. 888, we recognize that we took a different approach to stranded cost recovery associated with retail-turned-wholesale customers in

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Distribution Companies court noted, the Commission has given an LDC relief (and required the bypassing customer to bear its share of transition costs) if the LDC can show a direct nexus between the bypass and the pipeline, although the Commission has declined to adopt a generic rule addressing this issue. 88 F.3d at 1180-81.

United Illuminating, where we suggested that state and local regulatory authorities or the courts should be able to provide an adequate forum to address retail franchise matters, including recovery of stranded costs caused by municipalization, but said we would consider revisiting the question if United Illuminating could demonstrate the lack of a forum.[685] However, we explained that since the issuance of that decision we have had an opportunity to re-analyze the nature of the stranded cost problem when a retail customer **[30,407]** becomes a wholesale customer, including the potential that there might not be a state regulatory forum for recovery of such costs. In these circumstances, we have determined that where such costs are stranded as a direct result of Commission-mandated wholesale transmission access, these costs should be viewed as costs of the transition to competitive wholesale bulk power markets and this Commission should be the primary forum for addressing their recovery.

In response to Nucor's objection that there always is a state forum to address stranded cost recovery associated with retail-turned-wholesale customers, with the adequacy of the relief being a distinct issue, we clarify that our primary concern in retail-turned-wholesale situations is not whether there is an adequate state regulatory forum for the recovery of stranded costs associated with retail-turned-wholesale customers. Rather, our primary concern is that wholesale customers (whether or not formerly retail) should be responsible for the costs incurred to meet their power needs that are stranded when they use the wholesale transmission

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[685]63 FERC at pp. 62,583-84.

ordered by this Commission to reach new suppliers. Our decision to be the primary forum in the case of stranded costs associated with retail-turned-wholesale customers is based on the causal nexus between regulatory- mandated wholesale transmission access and the stranding of costs when a new municipal utility uses such access to obtain new power supply on behalf of retail customers previously served by the former supplying utility.

Rehearing Requests Seeking Expansion of Retail-Turned-Wholesale Jurisdiction

Other entities seek rehearing of the Commission's decision not to be the primary forum for stranded cost recovery in situations in which an existing municipal utility annexes territory served by another utility or otherwise expands its service territory.[686] A number of them argue that the loss of existing retail customers through municipal annexations or expansions is no different from the loss of retail customers through new municipalization because existing municipal systems are likely to use Commission-jurisdictional open access transmission to obtain resources to supply power to the annexed loads.[687] They submit that, just

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[686]*E.g.*, EEI, SoCal Edison, Centerior, Atlantic City, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Competition.

[687]*E.g.*, EEI, SoCal Edison, PSE&G, Puget, Public Service Co of CO, Coalition for Economic Competition. Coalition for Economic Competition suggests, for example, that villages and large industrial customers may opt to join existing municipal systems that, in most cases, will use Commission-jurisdictional

as with newly-municipalized customers, such costs would not be stranded but for the action of this Commission.

Some of these entities express concern that the Rule will encourage retail-turned-wholesale transactions to be undertaken as annexations rather than through the formation of new entities to avoid stranded costs.[688] Public Service Co of CO contends that Order No. 888, in conjunction with the Commission's section 211 order in American Municipal Power Ohio, Inc.,[689] may facilitate municipal annexations by enabling municipal systems to serve new territory through the establishment of second delivery points.

Coalition for Economic Competition and Puget also argue that the Commission must consider stranded costs that arise from municipal expansion in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. They contend that there is no justification for charging one rate to former retail customers taking transmission services through a new municipal utility and another rate to those taking service through municipal annexation or through use of another utility's transmission system.

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transmission tariffs to obtain resources to supply power to the annexed loads.

[688] *E.g.*, EEI, Coalition for Economic Competition, Atlantic City, Puget, Public Service Co of CO.

[689] 74 FERC ¶61,086, *final order directing transmission service*, 76 FERC ¶61,265 (1996).

PSE&G suggests that the distinction between new municipalization on the one hand and municipal annexation or expansion on the other hand may lead to unnecessary controversy and litigation as entities wrangle over whether a given expansion/annexation is really an expansion or a municipalization. It says that a situation could arise where a municipality **[30,408]** serves one town in order to serve thousands of additional customers in a second town. According to PSE&G, it is not clear from the Rule whether the Commission would consider this an expansion of a municipality's service territory or a new municipalization.

Puget submits that the stranded cost recovery mechanism must not be subject to being frustrated by simple artifices such as having the new supplier (instead of the departing customer) request and contract for transmission service. SoCal Edison seeks clarification of the Commission's authority to mandate stranded cost recovery if a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity (who in turn would interconnect with a neighboring jurisdictional utility). It asks the Commission to clarify that such a transaction effectively constitutes a municipalization, not an expansion of a service territory, and that the Commission, under FPA section 211, can compel the recovery of stranded costs by having the "new" jurisdictional utility assess a stranded cost charge and pass the revenues on to the utility from whose system the customer departed.

SoCal Edison seeks several additional clarifications. It states that it understands that the Commission's primary forum status in no way prevents or interferes with a state's authority to order stranded cost recovery from departing retail

customers. If this is not the case, SoCal Edison seeks rehearing on this issue. SoCal Edison also asks the Commission to clarify that the Commission retains the discretion to defer to a state stranded cost calculation methodology if appropriate to do so on the facts of a particular case.

Commission Conclusion

We have carefully reviewed the arguments made by petitioners seeking rehearing of our decision not to be the primary forum for stranded cost recovery in the case of municipal annexations. Based on that review we have decided to reconsider our decision. This conclusion is based in large part upon the very significant similarities between the creation of a *new* municipal utility system (also referred to as municipalization) and the expansion of an *existing* municipal utility system (*e.g.*, through annexation of additional retail service territory). We recognize that the *same nexus* to Commission-required transmission access that forms the basis for our decision to allow a utility to seek stranded cost recovery in cases of new municipalization -- use of the former supplying utility's transmission system -- is likely to be present in some cases of municipal annexation. In the case of both new municipalizations and annexations, the bundled retail customers of a local utility become the bundled retail customers of a municipal utility (in one case a new municipal utility, in the other an existing municipal utility) that *will use the transmission system of the retail customers' former supplier in order to access other suppliers.*

As we explain above, in a "retail-turned-wholesale customer" situation, such as the creation of a municipal utility

system, a Docket Nos. RM95-8-001 and RM94-7-002 newly-created entity becomes a wholesale power purchaser on behalf of the retail customers. It is the conduit by which retail customers, if they cannot obtain direct retail access, can reach power suppliers other than their historical local utility power supplier. Although the retail customers remain bundled retail customers, in that they become the bundled customers of the new entity, we call this a "retail-turned-wholesale customer" situation because the new entity in effect "stands in the shoes" of the retail customers for purposes of obtaining wholesale transmission access and new power supply. The same analogy applies to newly-annexed customers; they become "new" wholesale customers in the sense that the wholesale entity obtains transmission and new power supply on their behalf.

Accordingly, we clarify that this Commission will be the primary forum for addressing the recovery of stranded costs if an existing municipal utility uses the transmission system of its annexed retail customers' former supplier to access new suppliers to serve the annexed load. As long as Commission-required transmission access (the former supplier's open access tariff or transmission services ordered under FPA section 211) is the vehicle that enables an existing municipal utility to obtain power supplies to serve annexed loads, we believe that any costs stranded as a result of this wholesale transmission access are properly viewed as economic costs that are jurisdictional to this Commission. **[30,409]** In such a case, the bundled retail customers that are annexed by an existing municipal utility would, through the municipal utility, use the transmission system of their former supplier to obtain access to new supplies and thereby expose their former supplier to non-recovery of prudently incurred costs. As in the case of new municipal systems that use the

transmission system of their retail customers' former supplier, such costs would not be stranded *but for* the action of this Commission in requiring a utility to make unbundled transmission services available.[690]

Just as we will not be the primary forum for stranded cost recovery for all new municipalizations, so also we will not be the primary forum for stranded cost recovery for *all* cases of municipal annexation. Instead, our holding is limited to those cases in which the existing municipal system uses Commission-mandated transmission access from the annexed customers' former supplying utility to obtain power from a new supplier. Costs that are exposed to nonrecovery when an existing municipal utility does not use the transmission system of the retail customers' former supplier to reach a new generation supplier (*e.g.*, through self-generation or use of another utility's transmission system) do not meet the

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[690]SoCal Edison requests clarification that a transaction in which a retail customer disconnects from a utility's system and accesses another generation supplier by interconnecting with a public power entity, who in turn would interconnect with a neighboring jurisdictional utility, constitutes a municipalization, not an expansion of a service territory. Because we have decided to treat municipal annexations (or expansions) and new municipalizations similarly for purposes of stranded cost recovery under the Rule, SoCal Edison's request is moot to the extent that it envisions a scenario in which the former supplier's transmission system is used to access a new generation supplier. However, as discussed below, the Rule would not provide an opportunity to seek recovery of stranded costs if the municipal entity in the scenario described by SoCal Edison *does not* use the former supplier's transmission system.

definition of "wholesale stranded costs" for which the Rule provides an opportunity for recovery. Such costs are outside the scope of the Rule because such costs would not be stranded as a direct result of Commission-required transmission access.

We reject as misplaced the argument that the Commission, by failing to address costs that arise if a municipal utility (whether a new municipal utility or an existing municipal utility that annexes additional retail customer territory) does not use the historical supplying utility's transmission system, has not met its statutory obligation to "set just and reasonable" rates. The Commission in this rulemaking has not determined any utility's just and reasonable rates. Further, Order No. 888 does not by its terms bar the recovery of costs that do not result from the use of Commission-required transmission access. Utilities may, as before, seek recovery of such non-open access-related costs on a case-by-case basis in individual rate proceedings. The Commission will not prejudge those issues here.

As we indicated in Order No. 888 we also are concerned that there may be circumstances in which customers and/or utilities could attempt, through indirect use of open access transmission, to circumvent the ability of any regulatory commission -- either this Commission or state commissions -- to address recovery of stranded costs.[691] We reiterate that we reserve the right to address such situations on a case-by-case basis.

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[691] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at pp. 536-37.

We share the concern expressed by Puget that a retail-turned-wholesale customer should not be allowed to avoid any stranded cost obligation that it may have under Order No. 888 simply by having its new supplier be the entity that requests and contracts for transmission service from the former supplying utility. We clarify that the opportunity for recovery of stranded costs associated with retail-turned-wholesale customers under Order No. 888 applies if the transmission system of the former supplier is used to transmit the newly obtained power supplies to the departing retail customer, regardless of whether the customer or its new supplier is the actual entity that requests and contracts for the unbundled transmission service. We have revised the definition of "wholesale stranded cost" in section 35.26(b)(1)(ii) accordingly to include **[30,410]** the situation in which the retail customer subsequently becomes, either directly or through another wholesale transmission purchaser, an unbundled wholesale transmission services customer of the former supplying utility.

We clarify in response to SoCal Edison's request that our decision to be the primary forum for recovery of stranded costs from retail-turned-wholesale customers is not intended to prevent or to interfere with the authority of a state to permit any recovery from departing retail customers, such as by imposing an exit fee prior to creating the wholesale entity. As we indicated in Order No. 888, if the state has permitted any such recovery from a departing retail-turned-wholesale customer, that amount will not in fact be stranded. Accordingly, we will deduct that amount from the costs for

which the utility will be allowed to seek recovery from this Commission.[692]

We clarify in response to SoCal Edison's request that the Commission has the discretion to defer to a state stranded cost calculation methodology. However, because we recognize that state retail access plans may present questions that need to be addressed on a case-by-case basis, we will consider whether to exercise that discretion on a case-by-case basis.

7. Recovery of Stranded Costs Caused by Retail Wheeling

In Order No. 888, we concluded that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in order to reach a different generation supplier, and that utilities are entitled, from both a legal and a policy perspective, to an opportunity to recover all of their prudently incurred costs.[693] We explained that this Commission's authority to address retail stranded costs (i.e., stranded costs associated with retail wheeling customers) is based on our jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, and that the authority of state commissions to address retail stranded costs is based on their jurisdiction over local

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[692] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,819; *mimeo* at p. 537

[693] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,824-26; *mimeo* at pp. 553-58.

distribution facilities and the service of delivering electric energy to end users. Because it is a state decision to permit or to require the retail wheeling that causes stranded costs to occur, we decided we generally will leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority[694] does not have authority under state law to address stranded costs when the retail wheeling is required. In such a case, we will permit a utility to seek a customer- specific surcharge to be added to an unbundled transmission rate.

We noted that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We indicated that rates for services using facilities used in local distribution to make a retail sale are state-jurisdictional, and that states will be free to impose stranded costs caused retail wheeling on facilities or services used in local distribution. We also said that states may use their jurisdiction over local distribution facilities or services to recover so-called stranded benefits.

We stated that we believe our approach to stranded costs associated with retail wheeling customers represents an

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[694] "State regulatory authority" has the same meaning as provided in section 3(21) of the FPA: 'State regulatory authority' has the same meaning as the term 'State commission', except that in the case of an electric utility with respect to which the Tennessee Valley Authority has ratemaking authority (as defined in section 3 of the Public Utility Regulatory Policies Act of 1978), such term means the Tennessee Valley Authority.

appropriate balance between federal and state interests that ensures that the rates for transmission in interstate commerce by public utilities (except in a narrow circumstance) will not be burdened by retail costs.

We expressed concern about the cost-shifting potential in a holding company or other multi-state situation, where denial **[30,411]** of retail stranded cost recovery by a state regulatory authority could, through operation of the reserve equalization formula in a Commission-jurisdictional intra-system agreement, inappropriately shift the disallowed costs to affiliated operating companies in other states. We said that we will deal with such situations if they arise pursuant to public utility filings under section 205 or complaints under section 206. Thus, the need to amend a jurisdictional agreement to prevent stranded costs associated with retail wheeling customers from being shifted to customers in other states will be addressed on a case-by-case basis. We encouraged the affected state commissions in such situations to seek a mutually agreeable approach to this potential problem. If such a consensus solution resulted in a filing to modify a jurisdictional agreement, we indicated that we would accord such a proposal deference, particularly if other interested parties support the filing. In the event that the state commissions and other interested parties cannot reach consensus that would prevent cost shifting, we said that the Commission would ultimately have to resolve the appropriate treatment of such stranded costs.

Rehearing Requests Opposing Any Commission Involvement in Stranded Costs Associated With Retail Wheeling Customers

A number of entities dispute the Commission's statement that both it and the states have the legal authority to address stranded costs that result from retail wheeling. Central Illinois Light contends that the Commission's claim of dual jurisdiction is inconsistent with *FPC v. Southern California Edison Company*.[695] It says that the court in that case recognized that Congress meant to draw a bright line easily ascertained between state and federal jurisdiction, making unnecessary case-by-case analysis. Central Illinois Light asserts that the Commission has stepped over the bright line into the states' exclusive jurisdiction over retail rates.

IA Com seeks rehearing of the Commission's assertion of concurrent jurisdiction with state authorities over stranded costs associated with retail wheeling customers on the ground that it is based on the Commission's erroneous assertion of jurisdiction over unbundled retail transmission.

IL Com says that regardless of whether the Commission's claim of jurisdiction over retail transmission is upheld, the Commission's ruling that there is joint jurisdiction over retail stranded costs is in error. According to IL Com, the Commission has no authority over such stranded costs. IL Com also disputes the Commission's characterization of the derivation of state authority to address such stranded costs. It says that state commission authority does not derive only from states' jurisdiction over local distribution facilities and the

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[695] 376 U.S. 205, 215-16 (1964).

service of delivering electric energy to end users. IL Com submits that state commission authority to address retail stranded costs derives from the existence of state commission jurisdiction over the facilities and costs at the time of their incurrence.

A number of entities contend that Commission jurisdiction over transmission facilities used in interstate commerce does not give it jurisdiction over stranded investment in retail generating assets.[696] Several argue that the fact that a retail wheeling customer might need transmission access from its former supplier does not change the character of the costs that are stranded. They maintain that retail stranded costs are not costs of providing unbundled transmission service, but are costs associated with providing what was formerly bundled retail service, over which the Commission has no jurisdiction.[697]

Several entities argue that it is solely the action of the state that allows a given **[30,412]** utility's retail customers to

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[696] *E.g.*, Central Illinois Light, IN Consumer Counselor, IN Consumers, Nucor, FL Com, WI Com, VA Com, AR Com, MO/KS Com, OH Com, APPA. For example, FL Com asserts that costs for facilities that are currently under the jurisdiction of state authorities do not become the Commission's jurisdiction because retail wheeling is instituted; in most cases, the states approved both the construction and the cost recovery for these facilities under bundled rate structures. FL Com submits that the states are in a better position to judge the extent and value of assets that may become stranded as a result of retail wheeling.

[697] *E.g.*, APPA, AR Com, MO/KS Coms, OH Com.

seek alternative sources of supply; therefore, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime.[698]

A number of entities submit that the provision of FPA section 201 that federal regulation is "to extend only to those matters which are not subject to regulation by the States" bars any attempt by the Commission to displace or supplant an admittedly legitimate exercise of state authority over retail stranded costs.[699] NASUCA submits that all state commissions have the authority to establish just and reasonable rates for the retail electric utilities in their respective jurisdictions.[700] It maintains that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws; the Commission has no knowledge or expertise regarding the specific state legal frameworks in

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[698]*E.g.*, NARUC, TAPS.

[699]*E.g.*, NASUCA, NY Com, WY Com, NARUC. The Consumer's Utility Counsel Division of the Georgia Governor's Office of Consumer Affairs filed comments on June 24, 1996, in support of NARUC's request for rehearing on the jurisdictional issues pertaining to the recovery of retail stranded costs. While answers to requests for rehearing generally are not permitted, 18 CFR §385.213(a)(2) (1996), we will depart from our general rule because of the significant nature of this proceeding and will accept these comments.

[700]According to NASUCA, whether or not that authority includes a requirement that a utility receive 100 percent return on stranded costs (or something less) is a matter to be determined by the state courts and legislatures.

which these costs were included in rates. NY Com argues that the Commission does not have jurisdiction to determine the rate treatment of costs devoted to retail service and, thus, lacks authority to allow recovery if a state decides not to do so.

VA Com argues that section 201(b)(1) of the FPA restricts the Commission's jurisdiction to wholesale sales. It says that a departing retail customer remains a retail customer, regardless of the supplier. VA Com concludes that no portion of the transaction is a wholesale sale, and that there are no wholesale costs associated with a retail wheeling transaction.[701]

A number of entities seek rehearing of the Commission's decision that it will entertain stranded cost claims when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is[702] NARUC submits that Congress did not intend the Commission to become involved in adjudicating legal questions regarding the breadth of state law authority granted state commissions by their legislatures. NARUC expresses concern that the Commission would second-guess a state cost recovery determination and promote forum shopping. Once a balance has been struck at the state level

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[701] *See also* AR Com (one retail transaction is replaced by another retail transaction; there is no wholesale transaction and no wholesale costs over which the Commission has jurisdiction).

[702] *E.g.*, NARUC, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com.

concerning the terms of restructuring, NARUC submits that it is inconceivable that the Commission would have either the desire or authority to second-guess a state's legislative and regulatory processes.

Several entities object that the Commission effectively would authorize recovery of stranded costs associated with a retail wheeling customer if a state legislature withholds from the state regulatory agency the authority to approve stranded cost recovery.[703] They submit that just because a state has not given its regulatory commission the authority to impose stranded costs in the case of retail wheeling does not confer jurisdiction on the Commission to impose such charges. They contend that the state legislature should be the final arbiter of state policy. IL Com submits that if a state legislature chooses not to give its state commission the authority to act on stranded costs, "that can be taken as a clear indication that the state's legislature most certainly does not want FERC to address them."[704] Central Illinois Light objects that the Commission has offered no reason why it will accept the decision of the **[30,413]** regulatory agency, but not that of the legislature.

AMP-Ohio and Cleveland ask the Commission to clarify that its deference to the determinations of the states is to the authority of the states as exercised through state

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[703] *E.g.*, Central Illinois Light, IN Com, American Forest & Paper, IN Consumer Counselor, IN Consumers, IL Com. TX Com considers that it has the power to address stranded cost issues related to retail transmission service.

[704] IL Com at p. 38 (emphasis in original).

legislative bodies (and other political subdivisions with legislative authority) as well as to state regulatory bodies. They submit that if the state legislature, or a local government acting in accordance with its authority, enacts retail wheeling legislation that expressly limits the ability of its regulatory body to permit recovery of stranded costs, even barring all such recovery, the Commission should not become involved.

Several entities ask the Commission to clarify that Order No. 888 does not permit utilities to apply to the Commission for recovery of stranded costs associated with a retail wheeling customer when a state regulatory authority has "addressed" a request for the same stranded costs but has not allowed 100 percent recovery.[705] ELCON gives two hypothetical examples to which it asks the Commission to respond: one where a state regulatory authority possesses full stranded cost recovery authority but allows only 50 percent recovery; the other where the state legislature provides the state regulatory authority by statute with the power to permit recovery of up to 50 percent of identified stranded costs.

Commission Conclusion

We reaffirm our conclusion that both this Commission and the states have the legal authority to address stranded costs that result when retail customers obtain retail wheeling in interstate commerce from public utilities in order to reach a different generation supplier, but that, because it is a state decision to permit or require the retail wheeling that causes retail stranded costs to occur, we will leave it to state

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[705] *E.g.*, ELCON, NASUCA, IL Com, NY Com.

regulatory authorities to deal with any stranded costs occasioned by retail wheeling. The only circumstance in which we will entertain requests to recover stranded costs caused by retail wheeling is when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required.

We will reject the requests for rehearing that oppose any Commission involvement in stranded costs associated with retail wheeling customers. We disagree with those entities that challenge our conclusion that both this Commission and the states have the legal authority to address stranded costs that result from retail wheeling (variously described by those entities as dual, concurrent, or joint jurisdiction). The Commission explained in detail in Order No. 888 the legal basis for concluding that this Commission and the state commissions each have jurisdiction over separate aspects of a retail wheeling transaction.[706] This Commission has jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities. State commissions have jurisdiction over local distribution facilities and the service of delivering electric energy to end users. Based on our respective jurisdictions over separate aspects of the retail wheeling transaction, we believe either has the authority to provide the former supplying utility with an opportunity to recover costs stranded when the departing customer uses retail transmission in interstate commerce to reach a new supplier, but that here,

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[706] *See FERC Statutes and Regulations, Reulations Preambles January 1991-June 1996* at pp. 31,780-85; *mimeo* at pp. 427-42 and Appendix G.

unlike the retail-turned-wholesale scenario, the state commission should be the primary forum because these costs are stranded by the action of the state. We would act only if the primary forum is not available. We have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity to seek recovery of prudently incurred costs.

Several entities argue that the Commission does not have jurisdiction over stranded investment in retail generating assets, that use of Commission-jurisdictional transmission does not change the character of the costs that are stranded, that stranded costs associated with retail wheeling customers are not costs of providing unbundled transmission service, **[30, 414]** but are costs associated with providing what was formerly bundled retail service, and that only state regulators are in a position to rule on the treatment of costs that were allowed in retail rates pursuant to state laws. While we agree that stranded costs associated with retail wheeling are costs that are retail in character in the sense that they are in retail bundled rates and become stranded as a result of retail wheeling required by the state commission, we do not believe this precludes the Commission from exercising jurisdiction in the limited circumstances of the Rule.

As an initial matter, we note that there are rarely separate retail and wholesale generating facilities. Retail customers and wholesale requirements customers get energy from the same facilities, each buying a "slice of the system." Typically all generating assets go into both the retail and the wholesale rate bases for determining retail and wholesale rates. Rates are determined by allocating the total generating

costs among customer classes. The parties confuse the issue before us to the extent they suggest that state commissions, not this Commission, have "jurisdiction" over certain "costs." Neither the state commissions nor this Commission has exclusive jurisdiction over "costs." Each regulatory authority has jurisdiction to determine "rates" for services subject to its jurisdiction and, in determining rates, may take into account all of the costs incurred by the utility. Under historical cost-of-service ratemaking, each regulatory authority, in exercising its respective *ratemaking* jurisdiction, reviews the *total* costs incurred by a utility to provide service and makes its separate and independent determination of what costs may be recovered through rates within its jurisdiction.[707] Generating

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[707] If a utility is regulated by both this Commission and a state commission, each commission, in setting cost-of- service rates within its jurisdiction, will separately and independently determine the utility's total cost of providing service (also known as the utility's total revenue requirement). This will be based on the expenses incurred in providing service and a reasonable profit on the utility's assets that are used to provide the service. The commissions may differ as to what assets are appropriately included in total rate base, what other costs are appropriately included in the total cost of service, and what rate of return should be permitted. Once each regulatory authority has determined the appropriate total revenue requirement, it then will determine what portion of that total revenue requirement should be borne by the utility's wholesale customers and what share should be borne by retail customers (also called cost allocation). Each commission may also reach different conclusions on this split as well. Thus, under historical cost-based ratemaking, regulatory authorities do not carve out so-called "wholesale costs" that only this Commission can take into account in determining rates subject to its jurisdiction or so-called "retail costs" that only a state commission can take into account in

costs continually shift between retail and wholesale rates over time.[708]

More importantly, both the state commission and this Commission have a responsibility to oversee the financial health of the utilities we regulate. Each has jurisdiction to make judgments about recovery of the costs of the assets in the utility's total rate base. Utilities are entitled to a regulatory forum that can adjudicate claims that they are or are not entitled to recovery of costs incurred regardless of the initial retail or wholesale "character" of those costs, and we believe we have the authority and obligation to fill a regulatory "gap" that could occur.[709]

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determining rates subject to state jurisdiction. Additionally, this Commission and state commissions have the discretion to determine whether costs are appropriately recovered through a transmission, generation, or distribution component of a rate (also called functionalization of costs) within their respective jurisdictions.

[708]We reject arguments that stranded retail generation costs are not a cost of providing unbundled retail transmission. While such costs are not a cost of operating the physical transmission system, nevertheless, they are an economic cost incurred as a result of being required to provide retail transmission.

[709]This is not a regulatory "gap" in the sense that the Commission would be asserting authority over matters not within its jurisdiction. However, the Commission would be filling a regulatory "gap" to the extent that the utility normally would have the opportunity to seek approval from its state regulatory commission to recover costs in retail rates from a departing retail customer or to reallocate those costs to other retail customers. In circumstances where the utility does not have this opportunity

[30,415]

In response to the argument that it is solely the action of the state that allows a retail customer to seek alternative sources of supply and, as a result, there is no nexus between the Commission's wholesale transmission rule and any costs that might be stranded by a state-established customer choice regime, we agree. Indeed, as we indicate in Order No. 888, we decided to leave it to state regulatory authorities to deal with any stranded costs occasioned by retail wheeling (with a limited exception) because it is a state decision to permit or require the retail wheeling in the first instance that causes retail stranded costs to occur. Our determination, as explained above, is to fill any regulatory gap that arises as a result of interstate wheeling. We believe that it is necessary for the Commission to act as a backstop in this limited instance to ensure that costs stranded as a result of retail wheeling do not go unrecovered because the state regulatory authority lacks the authority under state law to address such costs. At the same time, as we stated in Order No. 888, we believe that most states have a number of mechanisms for addressing stranded costs caused by retail wheeling. We emphasize that this Rule is not intended to preempt the exercise of any existing state authority with respect to the assessment of a stranded cost or stranded benefits charge on a retail customer that obtains retail wheeling.

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because the state regulatory authority has no authority to address the issue, we may appropriately fill this regulatory "gap" to permit recovery from the departing customer through the retail transmission rate.

In response to arguments that the Commission's decision will result in second-guessing or interfering with a state's legislative processes and decisions, we believe these arguments are premature. As a general matter, we do not expect that our decision to be a backstop will interfere with legislative decisions that specifically address stranded cost matters and the scope of the state regulatory authority's authority in determining stranded costs. If states or parties to a retail stranded cost recovery case brought before this Commission believe that a Commission decision on the issue would interfere with state legislative decisions, they should raise their arguments, and support therefor, at that time.

We clarify that Order No. 888 does not permit utilities to seek recovery from the Commission of stranded costs associated with retail wheeling customers if a state regulatory authority with authority to address retail wheeling stranded costs has in fact addressed such costs, regardless of whether the state regulatory authority has allowed full recovery, partial recovery, or no recovery.

Rehearing Requests Supporting Broader Jurisdiction Over Stranded Costs Associated With Retail Wheeling Customers

A number of entities seek rehearing of the Commission's decision not to serve as a backstop for all stranded costs associated with retail wheeling customers. Some assert that the Commission has the legal authority to address independently stranded costs that arise from retail wheeling and that the Commission cannot lawfully abdicate or

delegate such authority to the states.[710] Coalition for Economic Competition submits that the Commission correctly concluded that it has jurisdiction over retail transmission rates, terms and conditions and the authority to address retail wheeling stranded costs. Thus, it argues that the Commission is without the power to make a "policy determination" that results in the Commission not exercising its legal authority over stranded costs associated with retail wheeling customers. It asserts that, just as the Commission recognizes that it "cannot simply turn over its jurisdiction" to the states to determine facilities subject to Commission jurisdiction,[711] the Commission cannot turn over its jurisdiction to establish stranded cost charges that it correctly determined it has the authority to establish. Coalition for Economic Competition argues that the Commission should adopt a stranded cost recovery policy similar to the policy the Commission has adopted with respect to the determination of state/federal jurisdiction, whereby the Commission would defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

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Utilities For Improved Transition argues that the Commission's authority over public utility rates for the transmission of electric power, both wholesale and retail, is plenary and exclusive. As a result, it submits that the Commission may not avoid responsibility for costs stranded

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[710] *E.g.*, Utilities For Improved Transition, Coalition for Economic Competition.

[711] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,784; *mimeo* at p. 439.

by transmission of retail power.[712] Illinois Power contends that Congress did not authorize the Commission to reject jurisdictional rate filings whenever the Commission regards the state commissions as a more convenient or appropriate forum.

EEI and the Coalition for Economic Competition contend that virtually all retail stranded costs can only occur through the vehicle of Commission-jurisdictional transmission in interstate commerce. They submit that the Commission, having recognized the clear nexus between FERC-jurisdictional transmission and stranded costs in the retail-turned-wholesale context, cannot fail to recognize the same clear nexus in the retail wheeling context.

Utilities For Improved Transition says that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states' doing so; the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service.

Coalition for Economic Competition and Utilities For Improved Transition contend that the Commission must

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[712]Utilities For Improved Transition argues that, based on *Consolidated Edison Company of New York, Inc.*, 15 FERC ¶61,174 at p. 61,405 (1981) and other cases, the Commission has jurisdiction over the entire delivery service (rendered on both the transmission and local distribution facilities) as a transmission transaction. Utilities For Improved Transition submits that states do not have authority over rates on local distribution facilities used to complete a transmission transaction.

consider stranded costs that arise from retail wheeling in order to satisfy its statutory obligation under the FPA to "set just and reasonable" rates. Coalition for Economic Competition maintains that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (e.g., wholesale wheeling and new municipalizations) but to exclude them from other jurisdictional wheeling rates (e.g., retail wheeling, municipal annexation, and bypass).[713] Utilities For Improved Transition says that the just and reasonable standard requires the Commission to backstop the states to ensure that there is full stranded cost recovery. It objects that Order No. 888's disposition of jurisdiction creates a problem of cross-class discrimination (wholesale versus retail) and inter-class discrimination (some retail versus the remainder of the retail).

Coalition for Economic Competition further argues that the Commission's failure to address all stranded costs associated with retail wheeling customers will result in an improper taking under the Constitution.[714] It also argues that the Commission is not permitted to disregard its findings in Order No. 888 which, according to Coalition for Economic Competition, "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail

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[713]EEI states that the Commission did not rebut EEI's argument that the Commission's failure to address all retail stranded costs was unduly discriminatory.

[714]In support of its argument, Coalition for Economic Competition cites *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591, 602 (1944); *Duquesne Light Company v. Barasch*, 488 U.S 299, 307-08 (1989).

wheeling, municipal annexation, and bypass stranded costs) is required.[715]

Illinois Power argues that the FPA does not authorize the Commission to discriminate among utilities based on the state of their residence, and that the Commission must allow all utilities to seek interstate rate recovery of just and reasonable retail stranded costs. Illinois Power asserts that the Rule will lead to the absurd, unduly discriminatory result that utilities located in states whose legislatures have failed to provide for stranded cost recovery will be better off than those located in states that provide for only limited stranded cost recovery. It supports use of the Commission's statutory authority to establish a uniform, national method for retail stranded cost recovery.

Coalition for Economic Competition also contends that the Commission's decision **[30,417]** to let the states deal with retail stranded costs is arbitrary and capricious because the Commission failed to consider the arguments that stranded cost opponents will make before state commissions, such as that a state lacks jurisdiction to impose stranded cost charges or that the state imposition of such charges may be preempted or found to be an undue burden on interstate commerce. It further argues that the Commission's reliance on state jurisdiction over the service of delivering electric energy to the end user does not reflect reasoned decisionmaking. It submits that the Commission has failed to consider that the sale of electric energy may take place outside of the state into which the energy is transmitted, in which case the state

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[715]Coalition for Economic Competition at p. 14.

commission may have no jurisdiction over either the sale or the transmission of the energy and, accordingly, no authority to consider stranded costs.

A number of entities ask the Commission to act on requests for retail stranded cost recovery when the state commission lacks authority or has authority to order recovery, but has declined to do so or has only allowed partial recovery.[716]

Lastly, TX Com notes that section 35.26(d) (dealing with recovery of retail stranded costs) refers only to public utilities. It suggests that the omission of a reference to transmitting utilities appears to be inadvertent and should be corrected.

Commission Conclusion

The Commission will reject the requests for rehearing of our decision not to assume a backstop role for all stranded costs associated with retail wheeling customers. We explained in Order No. 888 that commenters that describe our action as an unlawful abdication or delegation of authority misconstrue the nature of our decision to leave stranded costs associated with retail wheeling customers (with a limited exception) to state regulatory authorities.[717] We have not "abdicated" or

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[716]*E.g.*, Centerior, Southern, SoCal Edison.

[717]We also explained that the case law they cite (which they refer to again in their rehearing requests) to support the proposition that an agency is not authorized to abdicate its statutory responsibility or to delegate to parties and intervenors regulatory

"delegated" to state regulatory authorities our jurisdiction over the rates, terms, and conditions of retail transmission in interstate commerce; if retail transmission in interstate commerce by a public utility occurs, public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.[718] Instead, we have made a policy determination that the recovery of stranded costs associated with retail wheeling customers -- an issue over which either this Commission or state commissions could exercise authority by virtue of their jurisdiction over retail transmission in interstate commerce and over local distribution facilities and services, respectively -- is primarily a matter of local or state concern for which the primary forum

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responsibilities is factually distinguishable and inapposite. *See FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,825 and note 765; *mimeo* at pp. 554-55 and note 765.

[718]The entities who argue that the Commission has abdicated or delegated its jurisdiction to the states misconstrue the Commission's jurisdiction to determine rates for unbundled transmission in interstate commerce as somehow including exclusive "jurisdiction" over "costs." However, as discussed above, neither this Commission nor the state commissions has exclusive "jurisdiction" over "costs." Rather, each has jurisdiction to determine "rates" for services subject to its jurisdiction. It is in the course of determining "rates" for unbundled transmission in interstate commerce that this Commission can take into account various costs incurred by a utility to provide jurisdictional service. A state commission can take those same costs into account in making its separate and independent determinations of what costs may be recovered through rates within its jurisdiction. See note 707, supra, and accompanying text.

should be the state commissions. However, if the state regulatory authority does not have authority under state law to be the forum to address stranded costs when the retail wheeling is required, then we will entertain requests to recover such costs. As we explain above in response to the rehearing petitioners that oppose any Commission involvement in stranded costs associated with retail wheeling customers, we have made a policy decision that this Commission will step in to fill a regulatory "gap" that could result in no effective forum under which utilities would have an opportunity **[30,418]** to seek recovery of prudently incurred costs.[719]

We disagree with Coalition for Economic Competition's argument that our findings in Order No. 888 "inexorably" lead to the conclusion that Commission action on "all" stranded costs (including retail wheeling and bypass stranded costs) is required, much less that the Commission has ignored the findings in Order No. 888. To the contrary, as we explain in Section IV.J.1, it is not the purpose of this Rule to allow utilities an opportunity to seek to recover "all" uneconomic costs that might be stranded when a customer leaves its utility supplier. We have fully explained our reasons for adopting an approach that, for purposes of stranded cost recovery from wholesale transmission customers, relies on the nexus between stranded costs and the use of transmission tariffs required by this Commission and, for purposes of

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[719]Based on these same considerations, we reject Coalition for Economic Competition's request that the Commission assume a backstop role for all stranded costs associated with retail wheeling customers but defer to state stranded cost determinations so long as they are consistent with the Commission's policy.

stranded cost recovery from retail customers, recognizes state commission jurisdiction but fills potential regulatory gaps that could arise in the transition to new market structures.

We disagree with those entities that contend that the Commission must consider retail stranded costs in order to satisfy our statutory obligation under the FPA to set just and reasonable rates. In determining just and reasonable rates for jurisdictional transmission service, which currently are determined on a cost basis, the Commission satisfies its statutory obligation under the FPA by allowing utilities an opportunity to recover their prudently incurred costs plus a reasonable rate of return. As we have explained above, this may include the costs of use of the physical transmission system, as well as economic costs incurred by the utility when it provides Docket Nos. RM95-8-001 -92- and RM94-7-002 transmission service (e.g., stranded costs). However, in situations in which a state regulatory authority has the authority to address recovery of retail stranded costs, there is no regulatory "gap," and there is no obligation for this Commission to provide a second opportunity for recovery.[720]

We reject arguments that FPA sections 201, 205 and 206 do not give the Commission the flexibility to allow stranded costs in certain jurisdictional wheeling rates (wholesale wheeling and new municipalizations) but to

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[720]If the state regulatory authority is the forum before which to seek recovery, the utility may make whatever arguments it wishes regarding the justness and reasonableness of its rates, as well as any unconstitutional taking arguments it may have, before the state forum. Further, it can pursue appeals of unfavorable decisions through the state court system.

exclude them from other jurisdictional wheeling rates (retail wheeling in interstate commerce and use of another utility's transmission tariff), and that this policy somehow makes rates discriminatory. Recovery of this type of cost through a transmission rate is obviously not the norm, but is necessitated by the need to deal with the transition costs associated with this Rule. As discussed in detail in the Rule, the Commission has carefully balanced the interests of utilities as well as customers in concluding that the opportunity for stranded cost recovery through transmission rates should be permitted in only two general circumstances: (1) in the case of wholesale stranded costs, where there is a direct nexus to Commission-required transmission access; and (2) in the case of retail stranded costs, where there otherwise would be a regulatory gap because a state regulatory authority lacks authority under state law to address stranded costs at the time that retail wheeling is required. We see nothing in the FPA that precludes us from exercising this flexibility and, indeed, the parties have not pointed to anything that, in our opinion, precludes us from exercising this discretion.

We reject the argument that virtually all stranded costs associated with retail wheeling customers can occur only through the vehicle of Commission-jurisdictional transmission in interstate commerce, and therefore, that the same nexus between FERC-jurisdictional transmission and stranded costs that exists in the retail-turned-wholesale context is present in the retail wheeling context. We also **[30,419]** disagree that it is legally immaterial whether stranded costs are caused by the Commission's ordering the transmission or the states doing so, and that the determining factor is who has the jurisdiction to make the rates for the service, not who has the jurisdiction to order the service. The opportunity for stranded cost

recovery set forth in this Rule is based on the causal link between stranded costs and the availability and use of the Commission-required transmission tariff. It is true that in both the retail-turned-wholesale context and the retail wheeling context there is a limited nexus between stranded costs and Commission-jurisdictional access since, in both situations, the Commission has jurisdiction over the rates, terms and conditions of the transmission service and, therefore, the authority to permit stranded cost recovery through the transmission rates. However, the causal nexus to FERC-jurisdictional transmission and stranded costs in the two contexts (retail vs. retail-turned-wholesale) is different. In the retail wheeling context, there is no causal nexus between stranded costs and transmission that has been ordered by this Commission. In the retail-turned-wholesale context, in contrast, the opportunity for a utility to seek recovery of stranded costs is grounded on the existence of a direct causal nexus between stranded costs and transmission that has been *ordered by this Commission.*

We will reject the rehearing petitions that ask the Commission to act on requests for stranded cost recovery associated with retail wheeling customers not only when the state commission lacks authority, but also when the state commission has authority but either has declined to use it or has only allowed partial recovery. As explained above, our decision to entertain requests to recover stranded costs caused by retail wheeling in a limited circumstance (when the state regulatory authority does not have authority under state law to address stranded costs when the retail wheeling is required) is based on our determination to fill any regulatory gap that arises in association with interstate transmission.

We will reject TX Com's request that the Commission clarify that section 35.26(d) (dealing with recovery of retail stranded costs), which refers only to public utilities, should also refer to transmitting utilities. The Commission's decision to act as a limited backstop in the case of stranded costs associated with retail wheeling customers is based on our jurisdiction under sections 205 and 206 of the FPA over the rates, terms, and conditions of retail transmission in interstate commerce. As a result, our ability to allow the recovery of such costs through a surcharge on a section 205 unbundled transmission rate is necessarily limited to public utilities.[721]

Rehearing Requests Opposing Commission Treatment of Stranded Costs Associated with Retail Wheeling Customers in Holding Company Intra-system Agreement Cases

A number of entities oppose the Commission's proposal to address on a case-by-case basis whether jurisdictional intra-system agreements may need to be amended in order to prevent inappropriate cost-shifting that could occur if one state disallows stranded cost recovery associated with retail wheeling customers. IN Com objects that the problem is not the actions of one state or another, but rather the terms of the intra-system agreement.

AR Com objects that Order No. 888 is factually in error because a state's treatment of retail stranded costs under

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[721]We note that the definition of "retail stranded cost" in section 35.26(b)(5) mistakenly refers to "a public utility or transmitting utility" (emphasis added). We will revise the definition to remove the reference to "transmitting utility."

the Entergy System Agreement cannot shift costs to other jurisdictions.[722] It submits that whenever retail load changes, whether due to retail wheeling or any other factor, responsibility ratios under Entergy's reserve equalization schedule, MSS-1, will change and costs will shift irrespective of the regulator's treatment of retail stranded costs. AR Com says that MSS-1 reveals no changes in calculations due to retail treatment of stranded costs or any other retail ratemaking; only **[30,420]** "excess" capacity costs of intermediate gas- and oil-fired plant are "shifted" under the Entergy System Agreement. Although the Commission has the authority to amend intra-system agreements when wholesale cost allocations have become unjust and unreasonable, AR Com submits that the Commission does not have jurisdiction to reach to the state level and dictate what retail ratepayers should pay to shareholders. AR Com maintains that a FERC-jurisdictional intra-system agreement extends only to sales for resale (transactions among subsidiaries), and that if a holding company believes that an intra-system agreement is unduly discriminatory as a result of a state's disallowance of costs, the holding company can propose to amend it.[723]

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[722] *See also* MO/KS Coms (the cost-shifting problem does not arise because of a particular state treatment of stranded costs; it arises because Entergy insists on recovering 100 percent of its costs even when some portion of the costs are not economical).

[723] AR Com also objects to the Commission's description of the issue as involving not only holding companies, but also other multi-state situations. AR Com says that "[t]he mere fact that a company's territory crosses state lines does not automatically mean that all assets serve all customers, or that all customers are required to bear the economic risk associated with all assets, or that assets

AR Com argues that retail stranded costs fall to state jurisdiction regardless of whether the utility is a member of an interstate holding company. AR Com says that because the costs at issue are in retail rate base, any Commission influence over their recovery could occur only through preemption, but preemption of a state disallowance from retail rate base is possible only if there is a "trapped cost." AR Com submits that a disallowance of retail rate base cost cannot result in a trapped cost because there is no inconsistency between two agencies acting within their jurisdiction; the Commission has no jurisdiction to act. AR Com maintains that, unlike the Grand Gulf situation, the Commission has not mandated any Entergy generation costs into retail rate base. It further says that different state decisions regarding recovery of retail costs are not inconsistent decisions; they represent each state applying its law to its facts. According to AR Com, decisions by states leading to less than full recovery could be deemed inconsistent decisions only if there were a federal guarantee of full cost recovery of retail costs, which there is not.

AR Com and MO/KS Coms assert that the Commission's proposal for holding company situations cannot apply to future holding companies, where there is no history of joint planning justifying cost equalization, nor can it apply to future investments. They contend that this would require an assumption that the utility subsidiaries of a registered holding company have planned, and should plan, together rather than

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that at one time were solely state-jurisdictional can somehow, by virtue of a company's decision to expand across state lines, become FERC-jurisdictional." AR Com at p. 11.

separately (i.e., that interaffiliate transactions are always more efficient than nonaffiliate transactions), and that such assumption would be sound only if having the transaction occur between affiliates is inherently more efficient than having the transaction occur between an affiliate and a nonaffiliate.

Commission Conclusion

The comments raised for the most part are either premature or reflect a misunderstanding of the Commission's decision. Contrary to AR Com's argument, the Commission in Order No. 888 in no way asserted jurisdiction over state determinations of stranded costs associated with retail wheeling customers. We agree with AR Com that our jurisdiction extends only to sales for resale (and transmission in interstate commerce) and that a holding company can seek to amend an intra-system agreement if it believes the agreement is unduly discriminatory as a result of a state's disallowance of costs. However, a holding company also may seek to amend an agreement *before* any potential disallowances can occur, to keep cost-shifting from occurring. The fact is that intra-system agreements which involve wholesale sales among affiliate companies in different states could, through operation of their reserve equalization formulas, result in customers in one or more states having to indirectly bear stranded costs that are disallowed in another state, and the Commission has a responsibility to prevent inappropriate cost-shifting. Such determinations can be made only on a case-by-case basis. Again, as we stated in Order No. 888, we encourage affected state commissions to propose mutually agreeable solutions to this potential problem.

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8. Evidentiary Demonstration Necessary -- Reasonable Expectation Standard

In Order No. 888, the Commission concluded that a utility seeking to recover stranded costs must demonstrate that it had a reasonable expectation of continuing to serve a customer. We stated that whether a utility had a reasonable expectation of continuing to serve a customer, and for how long, will be determined on a case-by-case basis, and will depend on all of the facts and circumstances. We also determined that the existence of a notice provision in a contract would create a rebuttable presumption that the utility had no reasonable expectation of serving the customer beyond the specified period. We said that whether or not a contract contains an "evergreen" or other automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case.[724]

We also said that we would apply the reasonable expectation standard to retail-turned-wholesale customers. We explained that, before the Commission will permit a utility to recover stranded costs, the utility must demonstrate that it incurred such costs based on a reasonable expectation that the retail-turned-wholesale customer would continue to receive bundled retail service. Whether the state law awards exclusive service territories and imposes a mandatory obligation to serve would be among the factors to be considered in

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[724] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at pp. 570-72.

determining whether the reasonable expectation test is met in a particular case.[725]

We noted that Order No. 888 does not address who will bear the stranded costs caused by a departing generation customer if the Commission finds that the utility had no reasonable expectation of continuing to serve that customer. We indicated that we anticipate that, in such a case, a public utility will seek in subsequent requirements rate cases to have the costs reallocated among the remaining customers on its system. However, we stated that we were not prejudging that issue in the Rule.[726]

Rehearing Requests Opposing or Seeking Modification of the Reasonable Expectation Standard

APPA challenges the reasonable expectation standard as being too vague. It submits that the Commission has provided no guidance concerning application of the reasonable expectation standard, other than to state that it would decide the issue on a case-by-case basis. APPA objects that public utilities can exploit the uncertainty created by this standard, which will lead to costly and time-consuming litigation. IL Com supports replacing the reasonable expectation standard with a statutory, regulatory, contractual standard.

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[725]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at p. 572. We indicated that the same procedures would apply to retail customers that obtain retail wheeling.

[726]*FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at p. 31,831; *mimeo* at pp. 572-73.

Several entities contend that there is no basis to conclude that the reasonable expectation test could ever be met. VT DPS and Valero submit that, since 1973, utilities have known that a refusal to wheel power could subject them to antitrust liability. They say that Order No. 888 ignores the breadth of NRC licensing conditions. LEPA similarly argues that the reasonable expectation standard could not be met where NRC license conditions required an explicit wheeling commitment and prohibited the utility from including in the wheeling cost any amount attributable to the loss of customers due to the wheeling. It objects that delaying a decision on stranded cost recovery in such cases holds the threat of possible stranded cost charges over the heads of bulk power purchasers and thereby chills their ability to seek competitive sellers.

TAPS asserts that there should be an irrefutable presumption that no stranded costs are due from customers with pre-existing transmission rights, including customers who were the beneficiaries of NRC license conditions.[727] TAPS submits that there can be no legitimate "reasonable expectation" that such customers **[30,422]** would continue to purchase power if the price was higher than the market price.

Occidental Chemical asks the Commission to clarify that a utility could have had no reasonable expectation of recovering stranded costs from customers who, prior to the

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[727] AMP-Ohio submits that where transmission access and competition have existed to varying extents for decades, there should be an irrebuttable presumption of no reasonable expectation of continued service.

issuance of the NOPR, had the opportunity to switch to an alternative electric supplier or had the option of self-generating, obtaining on-site third-party generation, or municipalizing. Occidental Chemical further argues that it defies commercial expectations to allow a utility to argue that if a contract is silent on the issue of renewal, the obligation to purchase does not expire with the termination of the contract. It submits that the Commission has not shown that it has the authority to force customers to extend purchase agreements against their will in violation of accepted commercial practice.

A number of entities submit that the Commission erred in failing to treat a notice of termination provision as conclusive evidence that the utility had no reasonable expectation of continued service.[728] Several object that the Commission has failed to explain why the presence of a notice provision does not conclusively demonstrate the lack of a reasonable expectation and ipso facto terminate the obligation of the customer to purchase the product.[729] APPA objects that the Commission provided no evidence that it considered comments supporting making the presumption conclusive and that it found legally sufficient reasons to reject them.

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[728] *E.g.*, APPA, American Forest & Paper, Central Montana EC, NRECA, TDU Systems, Oglethorpe, IMPA, VT DPS, Valero, PA Munis.

[729] *E.g.*, APPA, NRECA, TDU Systems. See also VT DPS and Valero (by signing a contract with a termination date, the utility assumed the risk that the customer will elect to leave when the contract expires).

PA Munis objects that the rebuttable presumption represents an unjustified departure from the Commission's traditional policy of enforcing the express terms of notice provisions without any inquiry into the reasonable expectations of the party, provided that the agreements were negotiated in good faith and approved by the Commission.[730] PA Munis contends that wholesale requirements customers negotiated notice provisions with the knowledge that the Commission would enforce the notice provisions according to their terms, including the specific length of the term.[731] PA Munis argues that it is arbitrary and capricious to provide utilities an opportunity to seek to amend these contracts.

Several entities submit that the rebuttable presumption invites litigation and promotes uncertainty for customers.[732] APPA objects that the Commission has failed to establish the showing that it would require to overcome the presumption.

Referring to the Commission's discussion of evergreen provisions, Central Montana EC argues that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer

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[730]In support of its argument, PA Munis cites *Boston Edison Company*, 56 FPC 3414 (1976). *See also* American Forest & Paper.

[731]*Citing Kentucky Utilities Company*, 23 FERC ¶61,317 (1983); *Philadelphia Electric Company and Susquehanna Electric Company*, 65 FERC ¶61,303 (1993).

[732]*E.g.*, NRECA, IMPA, PA Munis.

than its initial term. Central Montana EC asserts that the presence of an evergreen provision infers simply that the parties agreed upon a mechanism to avoid the renegotiation of a power supply contract if, at the conclusion of its initial term, the parties were satisfied with the contract. It maintains that the parties' obligations are defined by the term and termination provisions of wholesale power contracts, and that the presence of a mechanism to avoid contract renegotiation does not alter those termination rights.

Commission Conclusion

We will reject the requests for rehearing of our decision to adopt a reasonable expectation standard to be applied on a case- by-case basis and to treat a notice provision in a contract as a rebuttable, not a conclusive, presumption of no reasonable expectation. Contrary to the claims of some entities, the Commission has explained the basis for its finding that utilities may have had an implicit obligation to serve their wholesale requirements customers and, therefore, that a utility should be given an opportunity to demonstrate that it incurred costs to provide **[30,423]** service to a customer and that it had a reasonable expectation that it would continue to serve the customer beyond the contract termination date. The same factors that some petitioners contend establish the absence of a reasonable expectation of continued service may be offered as evidence to be considered in determining whether the reasonable expectation test is met in a particular case.

We believe that our decision to treat a notice of termination provision in a contract as creating a rebuttable presumption that the utility had no reasonable expectation of

serving the customer beyond the period provided for in the notice provision is a reasonable one. It places evidentiary significance on the fact that a contract contains a notice of termination provision. Moreover, while it gives the utility an opportunity, based on the facts and circumstances of a particular case, to rebut the presumption of no reasonable expectation, it firmly places the burden of establishing reasonable expectation on the utility. Although some entities support treating notice provisions as a conclusive presumption of no reasonable expectation, as discussed below, we decline to adopt such an inflexible approach. Nevertheless, as we indicated in Order No. 888, when a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, we believe that the utility has a heavy burden in demonstrating that the contract ought to be modified.[733]

Contrary to the position of PA Munis, the rebuttable presumption is fully consistent with the Commission's past treatment of notice provisions. For example, the Kentucky Utilities Company case cited by PA Munis supports the proposition that, until a customer exercises a notice of termination provision, the utility is under an implicit obligation to continue to serve and plan for the future needs of the customer.[734] Thus, the presence of a notice of

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[733] *FERC Statutes and Regulations, Regulations Preambles January 1991-June 1996* at pp. 31,665, 31,813-14; *mimeo* at p. 87, 522.

[734] *See Kentucky Utilities Company*, 23 FERC at pp. 61,679-80 ("Once it receives an effective notice of cancellation, Kentucky can stop planning for the future needs of that customer. . . . To be

termination provision in a contract (particularly one not yet exercised by the customer), in and of itself, may not necessarily support the conclusion that the utility could never prove that it reasonably expected to continue serving the customer beyond the notice period.[735]

In response to APPA's objection that the Commission has failed to establish the showing that it would require to overcome the presumption, we note that the Commission cannot establish such a showing upfront because whether there is sufficient evidence to rebut the presumption of no reasonable expectation will depend on the facts of each case.

We appreciate the concerns expressed by some entities that the rebuttable presumption may increase the customer's uncertainty by inviting litigation. We have carefully weighed the pros and cons of treating a notice provision as a rebuttable presumption of no reasonable expectation versus the pros and cons of treating it as a conclusive presumption of no reasonable expectation. It is true, as some entities assert, that the rebuttable presumption approach presents the potential for litigation between the parties as to whether, in a particular case, the utility can rebut the presumption. The alternative

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effective a notice of cancellation must contain a specification of the source of supply, the date on which the source of supply will be available, and an affidavit from the supplier that it will supply the customer on the date the contract ends.").

[735]*See Potomac Electric Power Company*, 43 FERC ¶61,189 (1988) (suspending a notice of termination for five months due to questions about the impact of the proposed cancellation on service reliability).

would be to treat all contracts with notice of termination provisions as conclusive evidence that the utility could have had no reasonable expectation that it would continue to serve the customer beyond the specified notice period. While the latter approach presumably would reduce the number of cases in which the issue of a utility's reasonable expectation would have to be litigated, it would do so only by prohibiting a utility from ever demonstrating that, notwithstanding the existence of a notice provision, based on the facts of a particular case, the utility reasonably expected to continue serving the customer. While we do not prejudge the likelihood of a utility being able to rebut the presumption in a particular case, we believe that **[30,424]** it would not be in the public interest for the Commission to absolutely preclude a utility from being able to make such a showing. On this basis, we conclude that treating a notice provision as a rebuttable, rather than a conclusive, presumption that the utility did not have a reasonable expectation of continuing service to the customer is, on balance, the fairer and more equitable approach.

Central Montana EC asserts that it is wrong to infer from the existence of an automatic renewal provision that the parties intended that the contract might run longer than its initial term. However, our statement in Order No. 888 that the existence of an automatic renewal provision will be a factor to be considered in determining whether the presumption of no reasonable expectation is rebutted in a particular case makes no such inference. Whether the utility can rebut the presumption will depend on the facts of each case.

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I. Common Service Provisions

1 Definitions

1.1 Ancillary Services: Those services that are necessary to support the transmission of capacity and energy from resources to loads while maintaining reliable operation of the Transmission Provider's Transmission System in accordance with Good Utility Practice.

1.2 Annual Transmission Costs: The total annual cost of the Transmission System for purposes of Network Integration Transmission Service shall be the amount specified in Attachment H until amended by the Transmission Provider or modified by the Commission.

1.3 Application: A request by an Eligible Customer for transmission service pursuant to the provisions of the Tariff.

1.4 Commission: The Federal Energy Regulatory Commission.

1.5 Completed Application: An Application that satisfies all of the information and other requirements of the Tariff, including any required deposit.

1.6 Control Area: An electric power system or combination of electric power systems to which a common automatic generation control scheme is applied in order to:

(1) match, at all times, the power output of the generators within the electric power system(s) and capacity and energy purchased from entities (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 10 outside the electric power system(s), with the load within the electric power system(s);

(2) maintain scheduled interchange with other Control Areas, within the limits of Good Utility Practice;

(3) maintain the frequency of the electric power system(s) within reasonable limits in accordance with Good Utility Practice; and

(4) provide sufficient generating capacity to maintain operating reserves in accordance with Good Utility Practice.

1.7 Curtailment: A reduction in firm or non-firm transmission service in response to a transmission capacity **[30,508]** shortage as a result of system reliability conditions.

1.8 Delivering Party: The entity supplying capacity and energy to be transmitted at Point(s) of Receipt.

1.9 Designated Agent: Any entity that performs actions or functions on behalf of the Transmission Provider, an Eligible Customer, or the Transmission Customer required under the Tariff.

1.10 Direct Assignment Facilities: Facilities or portions of facilities that are constructed by the Transmission Provider for the sole use/benefit of a particular Transmission Customer requesting service under the Tariff. Direct Assignment Facilities shall be specified in the Service Agreement that governs service to the Transmission Customer and shall be subject to Commission approval.

1.11 Eligible Customer: (i) Any electric utility (including the Transmission Provider and any power marketer), Federal power marketing agency, or any person generating electric energy for sale for resale is an Eligible Customer under the Tariff. Electric energy sold or produced by such entity may be electric energy produced in the United States, Canada or Mexico. However, with respect to transmission service that the Commission is prohibited from ordering by Section 212(h) of the Federal Power Act, such entity is eligible only if the service is provided pursuant to a state requirement that the Transmission Provider offer the unbundled transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider. (ii) Any retail customer taking unbundled transmission service pursuant to a state requirement that the Transmission Provider offer the transmission service, or pursuant to a voluntary offer of such service by the Transmission Provider, is an Eligible Customer under the Tariff.

1.12 Facilities Study: An engineering study conducted by the Transmission Provider to determine the required modifications to the Transmission Provider's Transmission System, including the cost and scheduled completion date for such modifications, that will be required to provide the requested transmission service.

1.13 Firm Point-To-Point Transmission Service: Transmission Service under this Tariff that is reserved and/or scheduled between specified Points of Receipt and Delivery pursuant to Part II of this Tariff.

1.14 Good Utility Practice: Any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry during the relevant time period, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at a reasonable cost consistent with good business practices, reliability, safety and expedition. Good Utility Practice is not intended to be limited to the optimum practice, method, or act to the exclusion of all others, but rather to be acceptable practices, methods, or acts generally accepted in the region.

1.15 Interruption: A reduction in non-firm transmission service due to economic reasons pursuant to Section 14.7.

1.16 Load Ratio Share: Ratio of a Transmission Customer's Network Load to the Transmission Provider's total load computed in accordance with Sections 34.2 and 34.3 of the Network Integration Transmission Service under

Part III the Tariff and calculated on a rolling twelve month basis.

1.17 Load Shedding: The systematic reduction of system demand by temporarily decreasing load in response to transmission system or area capacity shortages, system instability, or voltage control considerations under Part III of the Tariff.

1.18 Long-Term Firm Point-To-Point Transmission Service: Firm Point-To-Point Transmission Service under Part II of the Tariff with a term of one year or more.

1.19 Native Load Customers: The wholesale and retail power customers of the Transmission Provider on whose behalf the Transmission Provider, by statute, franchise, regulatory requirement, or contract, has undertaken an obligation to construct and operate the Transmission Provider's system to meet the reliable electric needs of such customers.

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1.20 Network Customer: An entity receiving transmission service pursuant to the terms of the Transmission Provider's Network Integration Transmission Service under Part III of the Tariff.

1.21 Network Integration Transmission Service: The transmission service provided under Part III of the Tariff.

1.22 Network Load: The load that a Network Customer designates for Network Integration Transmission Service under Part III of the Tariff. The Network Customer's

Network Load shall include all load served by the output of any Network Resources designated by the Network Customer. A Network Customer may elect to designate less than its total load as Network Load but may not designate only part of the load at a discrete Point of Delivery. Where a Eligible Customer has elected not to designate a particular load at discrete points of delivery as Network Load, the Eligible Customer is responsible for making separate arrangements under Part II of the Tariff for any Point-To-Point Transmission Service that may be necessary for such non-designated load.

1.23 Network Operating Agreement: An executed agreement that contains the terms and conditions under which the Network Customer shall operate its facilities and the technical and operational matters associated with the implementation of Network Integration Transmission Service under Part III of the Tariff.

1.24 Network Operating Committee: A group made up of representatives from the Network Customer(s) and the Transmission Provider established to coordinate operating criteria and other technical considerations required for implementation of Network Integration Transmission Service under Part III of this Tariff.

1.25 Network Resource: Any designated generating resource owned, purchased or leased by a Network Customer under the Network Integration Transmission Service Tariff. Network Resources do not include any resource, or any portion thereof, that is committed for sale to third parties or otherwise cannot be called upon to meet the Network Customer's Network Load on a non-interruptible basis.

1.26 Network Upgrades: Modifications or additions to transmission-related facilities that are integrated with and support the Transmission Provider's overall Transmission System for the general benefit of all users of such Transmission System.

1.27 Non-Firm Point-To-Point Transmission Service: Point-To-Point Transmission Service under the Tariff that is reserved and scheduled on an as-available basis and is subject to Curtailment or Interruption as set forth in Section 14.7 under Part II of this Tariff. Non-Firm Point-To-Point Transmission Service is available on a stand-alone basis for periods ranging from one hour to one month.

1.28 Open Access Same-Time Information System (OASIS): The information system and standards of conduct contained in Part 37 of the Commission's regulations and all additional requirements implemented by subsequent Commission orders dealing with OASIS.

1.29 Part I: Tariff Definitions and Common Service Provisions contained in Sections 2 through 12.

1.30 Part II: Tariff Sections 13 through 27 pertaining to Point-To-Point Transmission Service in conjunction with the applicable Common Service Provisions of Part I and appropriate Schedules and Attachments.

1.31 Part III: Tariff Sections 28 through 35 pertaining to Network Integration Transmission Service in conjunction with the applicable Common Service Provisions of Part I and appropriate Schedules and Attachments.

1.32 Parties: The Transmission Provider and the Transmission Customer receiving service under the Tariff.

1.33 Point(s) of Delivery: Point(s) on the Transmission Provider's Transmission System where capacity and energy transmitted by the Transmission Provider will be made available to the Receiving Party under Part II of the Tariff. The Point(s) of Delivery shall be (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 17 specified in the Service Agreement for Long-Term Firm Point-To-Point Transmission Service.

1.34 Point(s) of Receipt: Point(s) of interconnection on the Transmission **[30,510]** Provider's Transmission System where capacity and energy will be made available to the Transmission Provider by the Delivering Party under Part II of the Tariff. The Point(s) of Receipt shall be specified in the Service Agreement for Long-Term Firm Point-To-Point Transmission Service.

1.35 Point-To-Point Transmission Service: The reservation and transmission of capacity and energy on either a firm or non-firm basis from the Point(s) of Receipt to the Point(s) of Delivery under Part II of the Tariff.

1.36 Power Purchaser: The entity that is purchasing the capacity and energy to be transmitted under the Tariff.

1.37 Receiving Party: The entity receiving the capacity and energy transmitted by the Transmission Provider to Point(s) of Delivery.

1.38 Regional Transmission Group (RTG): A voluntary organization of transmission owners, transmission users and other entities approved by the Commission to efficiently coordinate transmission planning (and expansion), operation and use on a regional (and interregional) basis.

1.39 Reserved Capacity: The maximum amount of capacity and energy that the Transmission Provider agrees to transmit for the Transmission Customer over the Transmission Provider's Transmission System between the Point(s) of Receipt and the Point(s) of Delivery under Part II of the Tariff. Reserved Capacity shall be expressed in terms of whole megawatts on a sixty (60) minute interval (commencing on the clock hour) basis.

1.40 Service Agreement: The initial agreement and any amendments or supplements thereto entered into by the Transmission Customer and the Transmission Provider for service under the Tariff.

1.41 Service Commencement Date: The date the Transmission Provider begins to provide service pursuant to the terms of an executed Service Agreement, or the date the Transmission Provider begins to provide service in accordance with Section 15.3 or Section 29.1 under the Tariff.

1.42 Short-Term Firm Point-To-Point Transmission Service: Firm Point-To-Point Transmission Service under Part II of the Tariff with a term of less than one year.

1.43 System Impact Study: An assessment by the Transmission Provider of (i) the adequacy of the Transmission

System to accommodate a request for either Firm Point-To-Point Transmission Service or Network Integration

Transmission Service and (ii) whether any additional costs may be incurred in order to provide transmission service.

1.44 Third-Party Sale: Any sale for resale in interstate commerce to a Power Purchaser that is not designated as part of Network Load under the Network Integration Transmission Service.

1.45 Transmission Customer: Any Eligible Customer (or its Designated Agent) that (i) executes a Service Agreement, or (ii) requests in writing that the Transmission Provider file with the Commission, a proposed unexecuted Service Agreement to receive transmission service under Part II of the Tariff. This term is used in the Part I Common Service Provisions to include customers receiving transmission service under Part II and Part III of this Tariff.

1.46 Transmission Provider: The public utility (or its Designated Agent) that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce and provides transmission service under the Tariff.

1.47 Transmission Provider's Monthly Transmission System Peak: The maximum firm usage of the Transmission Provider's Transmission System in a calendar month.

1.48 Transmission Service: Point-To-Point Transmission Service provided under Part II of the Tariff on a firm and non-firm basis.

1.49 Transmission System: The facilities owned, controlled or operated by the Transmission Provider that are used to provide transmission service under Part II and Part III of the Tariff.

2 Initial Allocation and Renewal Procedures

2.1 Initial Allocation of Available Transmission Capability: For purposes of determining whether existing **[30,511]** capability on the Transmission Provider's Transmission System is adequate to accommodate a request for firm service under this Tariff, all Completed Applications for new firm transmission service received during the initial sixty (60) day period commencing with the effective date of the Tariff will be deemed to have been filed simultaneously. A lottery system conducted by an independent party shall be used to assign priorities for Completed Applications filed simultaneously. All Completed Applications for firm transmission service received after the initial sixty (60) day period shall be assigned a priority pursuant to Section 13.2.

2.2 Reservation Priority For Existing Firm Service Customers: Existing firm service customers (wholesale requirements and transmission-only, with a contract term of one-year or more), have the right to continue to take transmission service from the Transmission Provider when the contract expires, rolls over or is renewed. This transmission reservation priority is independent of whether the existing customer continues to purchase capacity and energy from the Transmission Provider or elects to purchase capacity and energy from another supplier. If at the end of the contract term, the Transmission Provider's Transmission System cannot accommodate all of the requests for transmission

service the existing firm service customer must agree to accept a contract term at least equal to a competing request by any new Eligible Customer and to pay the current just and reasonable rate, as approved by the Commission, for such service. This transmission reservation priority for existing firm service customers is an ongoing right that may be exercised at the end of all firm contract terms of one-year or longer.

3 *Ancillary Services*

Ancillary Services are needed with transmission service to maintain reliability within and among the Control Areas affected by the transmission service. The Transmission Provider is required to provide (or offer to arrange with the local Control Area operator as discussed below), and the Transmission Customer is required to purchase, the following Ancillary Services (i) Scheduling, System Control and Dispatch, and (ii) Reactive Supply and Voltage Control from Generation Sources.

The Transmission Provider is required to offer to provide (or offer to arrange with the local Control Area operator as discussed below) the following Ancillary Services only to the Transmission Customer serving load within the Transmission Provider's Control Area (i) Regulation and Frequency Response, (ii) Energy Imbalance, (iii) Operating Reserve - Spinning, and (iv) Operating Reserve - Supplemental. The Transmission Customer serving load within the Transmission Provider's Control Area is required to acquire these Ancillary Services, whether from the Transmission Provider, from a third party, or by self-supply. The Transmission Customer may not decline the Transmission

Provider's offer of Ancillary Services unless it demonstrates that it has acquired the Ancillary Services from another source. The Transmission Customer must list in its Application which Ancillary Services it will purchase from the Transmission Provider.

If the Transmission Provider is a public utility providing transmission service but is not a Control Area operator, it may be unable to provide some or all of the Ancillary Services. In this case, the Transmission Provider can fulfill its obligation to provide Ancillary Services by acting as the Transmission Customer's agent to secure these Ancillary Services from the Control Area operator. The Transmission Customer may elect to (i) have the Transmission Provider act as its agent, (ii) secure the Ancillary Services directly from the Control Area operator, or (iii) secure the Ancillary Services (discussed in Schedules 3, 4, 5 and 6) from a third party or by self-supply when technically feasible.

The Transmission Provider shall specify the rate treatment and all related terms and conditions in the event of an unauthorized use of Ancillary Services by the Transmission Customer.

The specific Ancillary Services, prices and/or compensation methods are described on the Schedules that are attached to and made a part of the Tariff. Three principal requirements apply to discounts for Ancillary Services provided by the Transmission Provider in conjunction with its provision of transmission service **[30,512]** as follows: (1) any offer of a discount made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts

(including requests for use by one's wholesale merchant or an affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. A discount agreed upon for an Ancillary Service must be offered for the same period to all Eligible Customers on the Transmission Provider's system. Sections 3.1 through 3.6 below list the six Ancillary Services.

3.1 Scheduling, System Control and Dispatch Service: The rates and/or methodology are described in Schedule 1.

3.2 Reactive Supply and Voltage Control from Generation Sources Service: The rates and/or methodology are described in Schedule 2.

3.3 Regulation and Frequency Response Service: Where applicable the rates and/or methodology are described in Schedule 3.

3.4 Energy Imbalance Service: Where applicable the rates and/or methodology are described in Schedule 4.

3.5 Operating Reserve - Spinning Reserve Service: Where applicable the rates and/or methodology are described in Schedule 5.

3.6 Operating Reserve - Supplemental Reserve Service: Where applicable the rates and/or methodology are described in Schedule 6.

4 Open Access Same-Time Information System (OASIS)

Terms and conditions regarding Open Access Same-Time Information System and standards of conduct are set forth in 18 CFR §37 of the Commission's regulations (Open Access Same-Time Information System and Standards of Conduct for Public Utilities). In the event available transmission capability as posted on the OASIS is insufficient to accommodate a request for firm transmission service, additional studies may be required as provided by this Tariff pursuant to Sections 19 and 32.

5 Local Furnishing Bonds

5.1 Transmission Providers That Own Facilities Financed by Local Furnishing Bonds: This provision is applicable only to Transmission Providers that have financed facilities for the local furnishing of electric energy with tax-exempt bonds, as described in Section 142(f) of the Internal Revenue Code ("local furnishing bonds"). Notwithstanding any other provision of this Tariff, the Transmission Provider shall not be required to provide transmission service to any Eligible Customer pursuant to this Tariff if the provision of such transmission service would jeopardize the tax- exempt status of any local furnishing bond(s) used to finance the Transmission Provider's facilities that would be used in providing such transmission service.

5.2 Alternative Procedures for Requesting Transmission Service:

(i) If the Transmission Provider determines that the provision of transmission service requested by an Eligible

Customer would jeopardize the tax-exempt status of any local furnishing bond(s) used to finance its facilities that would be used in providing such transmission service, it shall (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 26 advise the Eligible Customer within thirty (30) days of receipt of the Completed Application.

(ii) If the Eligible Customer thereafter renews its request for the same transmission service referred to in (i) by tendering an application under Section 211 of the Federal Power Act, the Transmission Provider, within ten (10) days of receiving a copy of the Section 211 application, will waive its rights to a request for service under Section 213(a) of the Federal Power Act and to the issuance of a proposed order under Section 212(c) of the Federal Power Act. The Commission, upon receipt of the Transmission Provider's waiver of its rights to a request for service under Section 213(a) of the Federal Power Act and to the issuance of a proposed order under Section 212(c) of the Federal Power Act, shall issue an order under Section 211 of the Federal Power Act. Upon issuance of the order under Section 211 of the Federal Power Act, the Transmission Provider shall be required to provide the requested transmission service in accordance with the terms and conditions of this Tariff.

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6 *Reciprocity*

A Transmission Customer receiving transmission service under this Tariff agrees to provide comparable transmission service that it is capable of providing to the Transmission Provider on similar terms and conditions over facilities used for the transmission of electric energy owned,

controlled or operated by the Transmission Customer and over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer's corporate affiliates. A Transmission Customer that is a member of a power pool or Regional Transmission Group also agrees to provide comparable transmission service to the members of such power pool and Regional Transmission Group on similar terms and conditions over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer and over facilities used for the transmission of electric energy owned, controlled or operated by the Transmission Customer's corporate affiliates.

This reciprocity requirement applies not only to the Transmission Customer that obtains transmission service under the Tariff, but also to all parties to a transaction that involves the use of transmission service under the Tariff, including the power seller, buyer and any intermediary, such as a power marketer. This reciprocity requirement also applies to any Eligible Customer that owns, controls or operates transmission facilities that uses an intermediary, such as a power marketer, (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 28 to request transmission service under the Tariff. If the Transmission Customer does not own, control or operate transmission facilities, it must include in its Application a sworn statement of one of its duly authorized officers or other representatives that the purpose of its Application is not to assist an Eligible Customer to avoid the requirements of this provision.

7 Billing and Payment

7.1 Billing Procedure: Within a reasonable time after the first day of each month, the Transmission Provider shall submit an invoice to the Transmission Customer for the charges for all services furnished under the Tariff during the preceding month. The invoice shall be paid by the Transmission Customer within twenty (20) days of receipt. All payments shall be made in immediately available funds payable to the Transmission Provider, or by wire transfer to a bank named by the Transmission Provider.

7.2 Interest on Unpaid Balances: Interest on any unpaid amounts (including amounts placed in escrow) shall be calculated in accordance with the methodology specified for interest on refunds in the Commission's regulations at 18 C.F.R §35.19a(a)(2)(iii). Interest on delinquent amounts shall be calculated from the due date of the bill to the date of payment. When payments are made by mail, bills shall be considered as having been paid on the date of receipt by the Transmission Provider.

7.3 Customer Default: In the event the Transmission Customer fails, for any reason other than a billing dispute as described below, to make payment to the Transmission Provider on or before the due date as described above, and such failure of payment is not corrected within thirty (30) calendar days after the Transmission Provider notifies the Transmission Customer to cure such failure, a default by the Transmission Customer shall be deemed to exist. Upon the occurrence of a default, the Transmission Provider may initiate a proceeding with the Commission to terminate service but shall not terminate service until the Commission so

approves any such request. In the event of a billing dispute between the Transmission Provider and the Transmission Customer, the Transmission Provider will continue to provide service under the Service Agreement as long as the Transmission Customer (i) continues to make all payments not in dispute, and (ii) pays into an independent escrow account the portion of the invoice in dispute, pending resolution of such dispute. If the Transmission Customer fails to meet these two requirements for continuation of service, then the Transmission Provider may provide notice to the Transmission Customer of its intention to suspend service in sixty (60) days, in accordance with Commission policy.

8 *Accounting for the Transmission Provider's Use of the Tariff*

The Transmission Provider shall record the following amounts, as outlined below.

8.1 Transmission Revenues: Include in a separate operating revenue account or subaccount the revenues it receives from Transmission Service when making Third-Party Sales under Part II of the Tariff.

8.2 Study Costs and Revenues: Include in a separate transmission operating expense account or subaccount, costs properly chargeable to expense that are incurred to perform any System Impact Studies or Facilities Studies which the Transmission Provider conducts to determine if it must construct new transmission facilities or upgrades necessary for its own uses, including making Third-Party Sales under the Tariff; and include in a separate operating revenue account or

subaccount the revenues received for System Impact Studies or Facilities Studies performed when such amounts are separately stated and identified in the Transmission Customer's billing under the Tariff.

9 *Regulatory Filings*

Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the right of the Transmission Provider to unilaterally make application to the Commission for a change in rates, terms and conditions, charges, classification of service, Service Agreement, rule or regulation under Section 205 of the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

Nothing contained in the Tariff or any Service Agreement shall be construed as affecting in any way the ability of any Party receiving service under the Tariff to exercise its rights under the Federal Power Act and pursuant to the Commission's rules and regulations promulgated thereunder.

10 *Force Majeure and Indemnification*

10.1 Force Majeure: An event of Force Majeure means any act of God, labor disturbance, act of the public enemy, war, insurrection, riot, fire, storm or flood, explosion, breakage or accident to machinery or equipment, any Curtailment, order, regulation or restriction imposed by governmental military or lawfully established civilian authorities, or any other cause beyond a Party's control. A Force Majeure event does not include an act of negligence or

intentional wrongdoing. Neither the Transmission Provider nor the Transmission Customer will be considered in default as to any obligation under this Tariff if prevented from fulfilling the obligation due to an event of Force Majeure. However, a Party whose performance under this Tariff is hindered by an event of Force Majeure shall make all reasonable efforts to perform its obligations under this Tariff.

10.2 Indemnification: The Transmission Customer shall at all times indemnify, defend, and save the Transmission Provider harmless from, any and all damages, losses, claims, including claims and actions relating to injury to or death of any person or damage to property, demands, suits, recoveries, costs and expenses, court costs, attorney fees, and all other obligations by or to third parties, arising out of or resulting from the Transmission Provider s performance of its obligations under this Tariff on behalf of the Transmission Customer, except in cases of negligence or intentional wrongdoing by the Transmission Provider.

11 ***Creditworthiness***

For the purpose of determining the ability of the Transmission Customer to meet its obligations related to service hereunder, the Transmission Provider may require reasonable credit review procedures. This review shall be made in accordance with standard commercial practices. In addition, the Transmission Provider may require the Transmission Customer to provide and maintain in effect during the term of the Service Agreement, an unconditional and irrevocable letter of credit as security to meet its responsibilities and obligations under the Tariff, or an alternative form of security proposed by the Transmission

Customer and acceptable to the Transmission Provider and consistent with commercial practices established by the Uniform Commercial Code that protects the Transmission Provider against the risk of non-payment.

12 *Dispute Resolution Procedures*

12.1 Internal Dispute Resolution Procedures: Any dispute between a **[30,515]** Transmission Customer and the Transmission Provider involving transmission service under the Tariff (excluding applications for rate changes or other changes to the Tariff, or to any Service Agreement entered into under the Tariff, which shall be presented directly to the Commission for resolution) shall be referred to a designated senior representative of the Transmission Provider and a senior representative of the Transmission Customer for resolution on an informal basis as promptly as practicable. In the event the designated representatives are unable to resolve the dispute within thirty (30) days [or such other period as the Parties may agree upon] by mutual agreement, such dispute may be submitted to arbitration and resolved in accordance with the arbitration procedures set forth below.

12.2 External Arbitration Procedures: Any arbitration initiated under the Tariff shall be conducted before a single neutral arbitrator appointed by the Parties. If the Parties fail to agree upon a single arbitrator within ten (10) days of the referral of the dispute to arbitration, each Party shall choose one arbitrator who shall sit on a three-member arbitration panel. The two arbitrators so chosen shall within twenty (20) days select a third arbitrator to chair the arbitration panel. In either case, the arbitrators shall be knowledgeable in electric utility matters, including electric

transmission and bulk power issues, and shall not have any current or past substantial business or financial relationships with any party to the arbitration (except prior arbitration). The arbitrator(s) shall provide each of the Parties an opportunity to be heard and, except as otherwise provided herein, shall generally conduct the arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association and any applicable Commission regulations or Regional Transmission Group rules.

12.3 Arbitration Decisions: Unless otherwise agreed, the arbitrator(s) shall render a decision within ninety (90) days of appointment and shall notify the Parties in writing of such decision and the reasons therefor. The arbitrator(s) shall be authorized only to interpret and apply the provisions of the Tariff and any Service Agreement entered into under the Tariff and shall have no power to modify or change any of the above in any manner. The decision of the arbitrator(s) shall be final and binding upon the Parties, and judgment on the award may be entered in any court having jurisdiction. The decision of the arbitrator(s) may be appealed solely on the grounds that the conduct of the arbitrator(s), or the decision itself, violated the standards set forth in the Federal Arbitration Act and/or the Administrative Dispute Resolution Act. The final decision of the arbitrator must also be filed with the Commission if it affects jurisdictional rates, terms and conditions of service or facilities.

12.4 Costs: Each Party shall be responsible for its own costs incurred during the arbitration process and for the following costs, if applicable:

(A) the cost of the arbitrator chosen by the Party to sit on the three member panel and one half of the cost of the third arbitrator chosen; or

(B) one half the cost of the single arbitrator jointly chosen by the Parties.

12.5 Rights Under The Federal Power Act: Nothing in this section shall restrict the rights of any party to file a Complaint with the Commission under relevant provisions of the Federal Power Act.

II. Point-To-Point Transmission Service

Preamble

The Transmission Provider will provide Firm and Non-Firm Point-To-Point Transmission Service pursuant to the applicable terms and conditions of this Tariff. Point-To-Point Transmission Service is for the receipt of capacity and energy at designated Point(s) of Receipt and the transmission of such capacity and energy to designated Point(s) of Delivery.

13 *Nature of Firm Point-To-Point Transmission Service*

13.1 Term: The minimum term of Firm Point-To-Point Transmission Service shall be one day and the maximum term shall be specified in the Service Agreement.

13.2 Reservation Priority: Long-Term Firm Point-To-Point Transmission Service shall be available on a first-come, **[30,516]** first-served basis *i.e.*, in the chronological

sequence in which each Transmission Customer has reserved service. Reservations for Short-Term Firm Point-To-Point Transmission Service will be conditional based upon the length of the requested transaction. If the Transmission System becomes oversubscribed, requests for longer term service may preempt requests for shorter term service up to the following deadlines: one day before the commencement of daily service, one week before the commencement of weekly service, and one month before the commencement of monthly service. Before the conditional reservation deadline, if available transmission capability is insufficient to satisfy all Applications, an Eligible Customer with a reservation for shorter term service has the right of first refusal to match any longer term reservation before losing its reservation priority. A longer term competing request for Short-Term Firm Point-To-Point Transmission Service will be granted if the Eligible Customer with the right of first refusal does not agree to match the competing request within 24 hours (or earlier if necessary to comply with the scheduling deadlines provided in section 13.8) from being notified by the Transmission Provider of a longer-term competing request for Short-Term Firm Point-To-Point Transmission Service. After the conditional reservation deadline, service will commence pursuant to the terms of Part II of the Tariff. Firm Point-To-Point Transmission Service will always have a reservation priority over Non-Firm Point-To-Point Transmission Service under the Tariff. All Long-Term Firm Point-To-Point Transmission Service will have equal reservation priority with Native Load Customers and Network Customers. Reservation priorities for existing firm service customers are provided in Section 2.2.

13.3 Use of Firm Transmission Service by the Transmission Provider: The Transmission Provider will be subject to the rates, terms and conditions of Part II of the Tariff when making Third-Party Sales under (i) agreements executed on or after [insert date sixty (60) days after publication in Federal Register] or (ii) agreements executed prior to the aforementioned date that the Commission requires to be unbundled, by the date specified by the Commission. The Transmission Provider will maintain separate accounting, pursuant to Section 8, for any use of the Point-To-Point Transmission Service to make Third-Party Sales.

13.4 Service Agreements: The Transmission Provider shall offer a standard form Firm Point-To-Point Transmission Service Agreement (Attachment A) to an Eligible Customer when it submits a Completed Application for Long-Term Firm Point-To-Point Transmission Service. The Transmission Provider shall offer a standard form Firm Point-To-Point Transmission Service Agreement (Attachment A) to an Eligible Customer when it first submits a Completed Application for Short-Term Firm Point-To-Point Transmission Service pursuant to the Tariff. Executed Service Agreements that contain the information required under the Tariff shall be filed (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 40 with the Commission in compliance with applicable Commission regulations.

13.5 Transmission Customer Obligations for Facility Additions or Redispatch Costs: In cases where the Transmission Provider determines that the Transmission System is not capable of providing Firm Point-To-Point Transmission Service without (1) degrading or impairing the

reliability of service to Native Load Customers, Network Customers and other Transmission Customers taking Firm Point-To-Point Transmission Service, or (2) interfering with the Transmission Provider's ability to meet prior firm contractual commitments to others, the Transmission Provider will be obligated to expand or upgrade its Transmission System pursuant to the terms of Section 15.4. The Transmission Customer must agree to compensate the Transmission Provider for any necessary transmission facility additions pursuant to the terms of Section 27. To the extent the Transmission Provider can relieve any system constraint more economically by redispatching the Transmission Provider's resources than through constructing Network Upgrades, it shall do so, provided that the Eligible Customer agrees to compensate the Transmission Provider pursuant to the terms of Section 27. Any redispatch, Network Upgrade **[30,517]** or Direct Assignment Facilities costs (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 41 to be charged to the Transmission Customer on an incremental basis under the Tariff will be specified in the Service Agreement prior to initiating service.

13.6 Curtailment of Firm Transmission Service: In the event that a Curtailment on the Transmission Provider's Transmission System, or a portion thereof, is required to maintain reliable operation of such system, Curtailments will be made on a non-discriminatory basis to the transaction(s) that effectively relieve the constraint. If multiple transactions require Curtailment, to the extent practicable and consistent with Good Utility Practice, the Transmission Provider will curtail service to Network Customers and Transmission Customers taking Firm Point-To-Point Transmission Service on a basis comparable to the curtailment of service to the

Transmission Provider's Native Load Customers. All Curtailments will be made on a non-discriminatory basis, however, Non-Firm Point-To-Point Transmission Service shall be subordinate to Firm Transmission Service. When the Transmission Provider determines that an electrical emergency exists on its Transmission System and implements emergency procedures to Curtail Firm Transmission Service, the Transmission Customer shall make the required reductions upon request of the Transmission Provider. However, the Transmission Provider reserves the right to Curtail, in whole or in part, any Firm Transmission Service provided under the Tariff when, in the Transmission Provider's sole discretion, an emergency or other unforeseen condition impairs or degrades the reliability of its Transmission System. The Transmission Provider will notify all affected Transmission Customers in a timely manner of any scheduled Curtailments.

13.7 Classification of Firm Transmission Service:

(a) The Transmission Customer taking Firm Point-To- Point Transmission Service may (1) change its Receipt and Delivery Points to obtain service on a non-firm basis consistent with the terms of Section 22.1 or (2) request a modification of the Points of Receipt or Delivery on a firm basis pursuant to the terms of Section 22.2.

(b) The Transmission Customer may purchase transmission service to make sales of capacity and energy from multiple generating units that are on the Transmission Provider's Transmission System. For such a purchase of transmission service, the resources will be designated as multiple Points of Receipt, unless the multiple generating

units are at the same generating plant in which case the units would be treated as a single Point of Receipt.

(c) The Transmission Provider shall provide firm deliveries of capacity and energy from the Point(s) of Receipt to the Point(s) of Delivery. Each Point of Receipt at which firm transmission capacity is reserved by the Transmission Customer shall be set forth in the Firm Point-To-Point Service Agreement for Long-Term Firm Transmission Service along with a corresponding capacity reservation associated with each Point of Receipt. Points of Receipt and corresponding capacity reservations shall be as mutually agreed upon by the Parties for Short-Term Firm Transmission. Each Point of Delivery at which firm transmission capacity is reserved by the Transmission Customer shall be set forth in the Firm Point-To-Point Service Agreement for Long-Term Firm Transmission Service along with a corresponding capacity reservation associated with each Point of Delivery. Points of Delivery and corresponding capacity reservations shall be as mutually agreed upon by the Parties for Short-Term Firm Transmission. The greater of either (1) the sum of the capacity reservations at the Point(s) of Receipt, or (2) the sum of the capacity reservations at the Point(s) of Delivery shall be the Transmission Customer's Reserved Capacity. The Transmission Customer will be billed for its Reserved Capacity under the terms of Schedule 7. The Transmission Customer may not exceed its firm capacity reserved at each Point of Receipt and each Point of Delivery except as otherwise specified in Section 22. The Transmission Provider shall specify the rate treatment and all related terms and conditions applicable in the event that a Transmission Customer (including Third-Party Sales by the Transmission

Provider) **[30,518]** exceeds its firm reserved capacity at any Point of Receipt or Point of Delivery.

13.8 Scheduling of Firm Point-To-Point Transmission Service: Schedules for the Transmission Customer's Firm Point-To-Point Transmission Service must be submitted to the Transmission Provider no later than 10:00 a.m. [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] of the day prior to commencement of such service. Schedules submitted after 10:00 a.m. will be accommodated, if practicable. Hour-to-hour schedules of any capacity and energy that is to be delivered must be stated in increments of 1,000 kW per hour [or a reasonable increment that is generally accepted in the region and is consistently adhered to by the Transmission Provider]. Transmission Customers within the Transmission Provider's service area with multiple requests for Transmission Service at a Point of Receipt, each of which is under 1,000 kW per hour, may consolidate their service requests at a common point of receipt into units of 1,000 kW per hour for scheduling and billing purposes. Scheduling changes will be permitted up to twenty (20) minutes [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] before the start of the next clock hour provided that the Delivering Party and Receiving Party also agree to the schedule modification. The Transmission Provider will furnish to the Delivering Party's system operator, hour-to-hour schedules equal to those furnished by the Receiving Party (unless reduced for losses) and shall deliver the capacity and energy provided by such schedules. Should the Transmission Customer, Delivering Party or Receiving Party revise or terminate any schedule, such party shall immediately

notify the Transmission Provider, and the Transmission Provider shall have the right to adjust accordingly the schedule for capacity and energy to be received and to be delivered.

14 *Nature of Non-Firm Point-To-Point Transmission Service*

14.1 Term: Non-Firm Point-To-Point Transmission Service will be available for periods ranging from one (1) hour to one (1) month. However, a Purchaser of Non-Firm Point-To-Point Transmission Service will be entitled to reserve a sequential term of service (such as a sequential monthly term without having to wait for the initial term to expire before requesting another monthly term) so that the total time period for which the reservation applies is greater than one month, subject to the requirements of Section 18.3.

14.2 Reservation Priority: Non-Firm Point-To-Point Transmission Service shall be available from transmission capability in excess of that needed for reliable service to Native Load Customers, Network Customers and other Transmission Customers taking Long- Term and Short-Term Firm Point-To-Point Transmission Service. A higher priority will be assigned to reservations with a longer duration of service. In the event the Transmission System is constrained, competing requests of equal duration will be prioritized based on the highest price offered by the Eligible Customer for the Transmission Service. Eligible Customers that have already reserved shorter term service have the right of first refusal to match any longer term reservation before being preempted. A longer term competing request for Non-Firm Point-To-Point Transmission Service will be granted if the Eligible Customer with the right of first refusal does not agree to match the

competing request: (a) immediately for hourly Non-Firm Point-To-Point Transmission Service after notification by the Transmission Provider; and, (b) within 24 hours (or earlier if necessary to comply with the scheduling deadlines provided in section 14.6) for Non-Firm Point-To-Point Transmission Service other than hourly transactions after notification by the Transmission Provider. Transmission service for Network Customers from resources other than designated Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service. Non-Firm Point-To-Point Transmission Service over secondary Point(s) of Receipt and Point(s) of Delivery will have the lowest reservation priority under the Tariff.

14.3 Use of Non-Firm Point-To-Point Transmission Service by the [30,519] Transmission Provider: The Transmission Provider will be subject to the rates, terms and conditions of Part II of the Tariff when making Third-Party Sales under (i) agreements executed on or after [insert date (Name of Transmission Provider) Open Access Transmission Tariff Original Sheet No. 48 sixty (60) days after publication in Federal Register] or (ii) agreements executed prior to the aforementioned date that the Commission requires to be unbundled, by the date specified by the Commission. The Transmission Provider will maintain separate accounting, pursuant to Section 8, for any use of Non-Firm Point-To-Point Transmission Service to make Third-Party Sales.

14.4 Service Agreements: The Transmission Provider shall offer a standard form Non-Firm Point-To-Point Transmission Service Agreement (Attachment B) to an Eligible Customer when it first submits a Completed Application for Non-Firm Point-To-Point Transmission

Service pursuant to the Tariff. Executed Service Agreements that contain the information required under the Tariff shall be filed with the Commission in compliance with applicable Commission regulations.

14.5 Classification of Non-Firm Point-To-Point Transmission Service: Non-Firm Point-To-Point Transmission Service shall be offered under terms and conditions contained in Part II of the Tariff. The Transmission Provider undertakes no obligation under the Tariff to plan its Transmission System in order to have sufficient capacity for Non-Firm Point-To-Point Transmission Service. Parties requesting Non-Firm Point-To-Point Transmission Service for the transmission of firm power do so with the full realization that such service is subject to availability and to Curtailment or Interruption under the terms of the Tariff. The Transmission Provider shall specify the rate treatment and all related terms and conditions applicable in the event that a Transmission Customer (including Third- Party Sales by the Transmission Provider) exceeds its non-firm capacity reservation. Non-Firm Point-To-Point Transmission Service shall include transmission of energy on an hourly basis and transmission of scheduled short-term capacity and energy on a daily, weekly or monthly basis, but not to exceed one month's reservation for any one Application, under Schedule 8.

14.6 Scheduling of Non-Firm Point-To-Point Transmission Service: Schedules for Non-Firm Point-To-Point Transmission Service must be submitted to the Transmission Provider no later than *2:00 p.m.* [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] of the

day prior to commencement of such service. Schedules submitted after 2:00 p.m. will be accommodated, if practicable. Hour-to-hour schedules of energy that is to be delivered must be stated in increments of 1,000 kW per hour [or a reasonable increment that is generally accepted in the region and is consistently adhered to by the Transmission Provider]. Transmission Customers within the Transmission Provider's service area with multiple requests for Transmission Service at a Point of Receipt, each of which is under 1,000 kW per hour, may consolidate their schedules at a common Point of Receipt into units of 1,000 kW per hour. Scheduling changes will be permitted up to *twenty (20) minutes* [or a reasonable time that is generally accepted in the region and is consistently adhered to by the Transmission Provider] before the start of the next clock hour provided that the Delivering Party and Receiving Party also agree to the schedule modification. The Transmission Provider will furnish to the Delivering Party's system operator, hour-to-hour schedules equal to those furnished by the Receiving Party (unless reduced for losses) and shall deliver the capacity and energy provided by such schedules. Should the Transmission Customer, Delivering Party or Receiving Party revise or terminate any schedule, such party shall immediately notify the Transmission Provider, and the Transmission Provider shall have the right to adjust accordingly the schedule for capacity and energy to be received and to be delivered.

14.7 Curtailment or Interruption of Service: The Transmission Provider reserves the right to Curtail, in whole or in part, Non-Firm Point-To-Point Transmission Service provided under the Tariff for reliability reasons when, an emergency or other unforeseen condition threatens to impair

or degrade **[30,520]** the reliability of its Transmission System. The Transmission Provider reserves the right to Interrupt, in whole or in part, Non-Firm Point-To-Point Transmission Service provided under the Tariff for economic reasons in order to accommodate (1) a request for Firm Transmission Service, (2) a request for Non- Firm Point-To-Point Transmission Service of greater duration, (3) a request for Non-Firm Point-To-Point Transmission Service of equal duration with a higher price, or (4) transmission service for Network Customers from non-designated resources. The Transmission Provider also will discontinue or reduce service to the Transmission Customer to the extent that deliveries for transmission are discontinued or reduced at the Point(s) of Receipt. Where required, Curtailments or Interruptions will be made on a non- discriminatory basis to the transaction(s) that effectively relieve the constraint, however, Non-Firm Point-To-Point Transmission Service shall be subordinate to Firm Transmission Service. If multiple transactions require Curtailment or Interruption, to the extent practicable and consistent with Good Utility Practice, Curtailments or Interruptions will be made to transactions of the shortest term (*e.g.*, hourly non- firm transactions will be Curtailed or Interrupted before daily non-firm transactions and daily non-firm transactions will be Curtailed or Interrupted before weekly non-firm transactions). Transmission service for Network Customers from resources other than designated Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service under the Tariff. Non-Firm Point-To-Point Transmission Service over secondary Point(s) of Receipt and Point(s) of Delivery will have a lower priority than any Non-Firm Point-To-Point Transmission Service under the Tariff. The Transmission Provider will provide advance notice of Curtailment or

Interruption where such notice can be provided consistent with Good Utility Practice.

15 *Service Availability*

15.1 General Conditions: The Transmission Provider will provide Firm and Non-Firm Point-To-Point Transmission Service over, on or across its Transmission System to any Transmission Customer that has met the requirements of Section 16.

15.2 Determination of Available Transmission Capability: A description of the Transmission Provider's specific methodology for assessing available transmission capability posted on the Transmission Provider's OASIS (Section 4) is contained in Attachment C of the Tariff. In the event sufficient transmission capability may not exist to accommodate a service request, the Transmission Provider will respond by performing a System Impact Study.

15.3 Initiating Service in the Absence of an Executed Service Agreement: If the Transmission Provider and the Transmission Customer requesting Firm or Non-Firm Point-To-Point Transmission Service cannot agree on all the terms and conditions of the Point-To-Point Service Agreement, the Transmission Provider shall file with the Commission, within thirty (30) days after the date the Transmission Customer provides written notification directing the Transmission Provider to file, an unexecuted Point-To-Point Service Agreement containing terms and conditions deemed appropriate by the Transmission Provider for such requested Transmission Service. The Transmission Provider shall commence providing Transmission Service subject to the

Transmission Customer agreeing to (i) compensate the Transmission Provider at whatever rate the Commission ultimately determines to be just and reasonable, and (ii) comply with the terms and conditions of the Tariff including posting appropriate security deposits in accordance with the terms of Section 17.3.

15.4 Obligation to Provide Transmission Service that Requires Expansion or Modification of the Transmission System: If the Transmission Provider determines that it cannot accommodate a Completed Application for Firm Point-To-Point Transmission Service because of insufficient capability on its Transmission System, the Transmission Provider will use due diligence to expand or modify its Transmission System to provide the requested Firm Transmission Service, provided the Transmission Customer agrees to compensate the Transmission **[30,521]** Provider for such costs pursuant to the terms of Section 27. The Transmission Provider will conform to Good Utility Practice in determining the need for new facilities and in the design and construction of such facilities. The obligation applies only to those facilities that the Transmission Provider has the right to expand or modify.

15.5 Deferral of Service: The Transmission Provider may defer providing service until it completes construction of new transmission facilities or upgrades needed to provide Firm Point-To-Point Transmission Service whenever the Transmission Provider determines that providing the requested service would, without such new facilities or upgrades, impair or degrade reliability to any existing firm services.

15.6 Other Transmission Service Schedules: Eligible Customers receiving transmission service under other agreements on file with the Commission may continue to receive transmission service under those agreements until such time as those agreements may be modified by the Commission.

15.7 Real Power Losses: Real Power Losses are associated with all transmission service. The Transmission Provider is not obligated to provide Real Power Losses. The Transmission Customer is responsible for replacing losses associated with all transmission service as calculated by the Transmission Provider. The applicable Real Power Loss factors are as follows: [To be completed by the Transmission Provider].

16 *Transmission Customer Responsibilities*

16.1 Conditions Required of Transmission Customers: Point-To-Point Transmission Service shall be provided by the Transmission Provider only if the following conditions are satisfied by the Transmission Customer:

a. The Transmission Customer has pending a Completed Application for service;

b. The Transmission Customer meets the creditworthiness criteria set forth in Section 11;

c. The Transmission Customer will have arrangements in place for any other transmission service necessary to effect the delivery from the generating source to

the Transmission Provider prior to the time service under Part II of the Tariff commences;

d. The Transmission Customer agrees to pay for any facilities constructed and chargeable to such Transmission Customer under Part II of the Tariff, whether or not the Transmission Customer takes service for the full term of its reservation; and

e. The Transmission Customer has executed a Point-To- Point Service Agreement or has agreed to receive service pursuant to Section 15.3.

16.2 Transmission Customer Responsibility for Third-Party Arrangements: Any scheduling arrangements that may be required by other electric systems shall be the responsibility of the Transmission Customer requesting service. The Transmission Customer shall provide, unless waived by the Transmission Provider, notification to the Transmission Provider identifying such systems and authorizing them to schedule the capacity and energy to be transmitted by the Transmission Provider pursuant to Part II of the Tariff on behalf of the Receiving Party at the Point of Delivery or the Delivering Party at the Point of Receipt. However, the Transmission Provider will undertake reasonable efforts to assist the Transmission Customer in making such arrangements, including without limitation, providing any information or data required by such other electric system pursuant to Good Utility Practice.

17 *Procedures for Arranging Firm Point-To-Point Transmission Service*

17.1 Application: A request for Firm Point-To-Point Transmission Service for periods of one year or longer must contain a written Application to: [Transmission Provider Name and Address], at least sixty (60) days in advance of the calendar month in which service is to commence. The Transmission Provider will consider requests for such firm service on shorter notice when feasible. Requests for firm service for periods of less than one year shall be subject to expedited procedures that shall be negotiated between the Parties within the time constraints provided in Section 17.5. All Firm Point-To-Point Transmission Service requests should **[30,522]** be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required information to the Transmission Provider by telefax, or (ii) providing the information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the priority of the Application.

17.2 Completed Application: A Completed Application shall provide all of the information included in 18 CFR 2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the entity requesting service;

(ii) A statement that the entity requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) The location of the Point(s) of Receipt and Point(s) of Delivery and the identities of the Delivering Parties and the Receiving Parties;

(iv) The location of the generating facility(ies) supplying the capacity and energy and the location of the load ultimately served by the capacity and energy transmitted. The Transmission Provider will treat this information as confidential except to the extent that disclosure of this information is required by this Tariff, by regulatory or judicial order, for reliability purposes pursuant to Good Utility Practice or pursuant to RTG transmission information sharing agreements. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations;

(v) A description of the supply characteristics of the capacity and energy to be delivered;

(vi) An estimate of the capacity and energy expected to be delivered to the Receiving Party;

(vii) The Service Commencement Date and the term of the requested Transmission Service; and

(viii) The transmission capacity requested for each Point of Receipt and each Point of Delivery on the Transmission Provider's Transmission System; customers may combine their requests for service in order to satisfy the

minimum transmission capacity requirement. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

17.3 Deposit: A Completed Application for Firm Point-To-Point Transmission Service also shall include a deposit of either one month's charge for Reserved Capacity or the full charge for Reserved Capacity for service requests of less than one month. If the Application is rejected by the Transmission Provider because it does not meet the conditions for service as set forth herein, or in the case of requests for service arising in connection with losing bidders in a Request For Proposals (RFP), said deposit shall be returned with interest less any reasonable costs incurred by the Transmission Provider in connection with the review of the losing bidder's Application. The deposit also will be returned with interest less any reasonable costs incurred by the Transmission Provider if the Transmission Provider is unable to complete new facilities needed to provide the service. If an Application is withdrawn or the Eligible Customer decides not to enter into a Service Agreement for Firm Point-To-Point Transmission Service, the deposit shall be refunded in full, with interest, less reasonable costs incurred by the Transmission Provider to the extent such costs have not already been recovered by the Transmission Provider from the Eligible Customer. The Transmission Provider will provide to the Eligible Customer a complete accounting of all costs deducted from the refunded deposit, which the Eligible Customer may contest if there is a dispute concerning the deducted costs. Deposits associated with construction of new facilities are subject to the provisions of Section 19. If a Service Agreement for Firm Point-To-Point Transmission

Service is executed, the deposit, with interest, will be returned to the Transmission Customer upon expiration **[30,523]** or termination of the Service Agreement for Firm Point-To-Point Transmission Service. Applicable interest shall be computed in accordance with the Commission's regulations at 18 CFR §35.19a(a)(2)(iii), and shall be calculated from the day the deposit check is credited to the Transmission Provider's account.

17.4 Notice of Deficient Application: If an Application fails to meet the requirements of the Tariff, the Transmission Provider shall notify the entity requesting service within fifteen (15) days of receipt of the reasons for such failure. The Transmission Provider will attempt to remedy minor deficiencies in the Application through informal communications with the Eligible Customer. If such efforts are unsuccessful, the Transmission Provider shall return the Application, along with any deposit, with interest. Upon receipt of a new or revised Application that fully complies with the requirements of Part II of the Tariff, the Eligible Customer shall be assigned a new priority consistent with the date of the new or revised Application.

17.5 Response to a Completed Application: Following receipt of a Completed Application for Firm Point-To-Point Transmission Service, the Transmission Provider shall make a determination of available transmission capability as required in Section 15.2. The Transmission Provider shall notify the Eligible Customer as soon as practicable, but not later than thirty (30) days after the date of receipt of a Completed Application either (i) if it will be able to provide service without performing a System Impact Study or (ii) if such a study is needed to evaluate the impact of the

Application pursuant to Section 19.1. Responses by the Transmission Provider must be made as soon as practicable to all completed applications (including applications by its own merchant function) and the timing of such responses must be made on a non-discriminatory basis.

17.6 Execution of Service Agreement: Whenever the Transmission Provider determines that a System Impact Study is not required and that the service can be provided, it shall notify the Eligible Customer as soon as practicable but no later than thirty (30) days after receipt of the Completed Application. Where a System Impact Study is required, the provisions of Section 19 will govern the execution of a Service Agreement. Failure of an Eligible Customer to execute and return the Service Agreement or request the filing of an unexecuted service agreement pursuant to Section 15.3, within fifteen (15) days after it is tendered by the Transmission Provider will be deemed a withdrawal and termination of the Application and any deposit submitted shall be refunded with interest. Nothing herein limits the right of an Eligible Customer to file another Application after such withdrawal and termination.

17.7 Extensions for Commencement of Service: The Transmission Customer can obtain up to *five (5) one-year extensions* for the commencement of service. The Transmission Customer may postpone service by paying a non-refundable annual reservation fee equal to one- month's charge for Firm Transmission Service for each year or fraction thereof. If during any extension for the commencement of service an Eligible Customer submits a Completed Application for Firm Transmission Service, and such request can be satisfied only by releasing all or part of

the Transmission Customer's Reserved Capacity, the original Reserved Capacity will be released unless the following condition is satisfied. Within thirty (30) days, the original Transmission Customer agrees to pay the Firm Point-To-Point transmission rate for its Reserved Capacity concurrent with the new Service Commencement Date. In the event the Transmission Customer elects to release the Reserved Capacity, the reservation fees or portions thereof previously paid will be forfeited.

18 ***Procedures for Arranging Non-Firm Point-To-Point Transmission Service***

18.1 Application: Eligible Customers seeking Non-Firm Point-To-Point Transmission Service must submit a Completed Application to the Transmission Provider. Applications should be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required **[30,524]** information to the Transmission Provider by telefax, or (ii) providing the information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the service priority of the Application.

18.2 Completed Application: A Completed Application shall provide all of the information included in 18 CFR §2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the entity requesting service;

(ii) A statement that the entity requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) The Point(s) of Receipt and the Point(s) of Delivery;

(iv) The maximum amount of capacity requested at each Point of Receipt and Point of Delivery; and

(v) The proposed dates and hours for initiating and terminating transmission service hereunder.

In addition to the information specified above, when required to properly evaluate system conditions, the Transmission Provider also may ask the Transmission Customer to provide the following:

(vi) The electrical location of the initial source of the power to be transmitted pursuant to the Transmission Customer's request for service; and

(vii) The electrical location of the ultimate load.

The Transmission Provider will treat this information in (vi) and (vii) as confidential at the request of the Transmission Customer except to the extent that disclosure of this information is required by this Tariff, by regulatory or judicial order, for reliability purposes pursuant to Good Utility Practice, or pursuant to RTG transmission information sharing agreements. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

18.3 Reservation of Non-Firm Point-To-Point Transmission Service: Requests for monthly service shall be submitted *no earlier than sixty (60) days* before service is to commence; requests for weekly service shall be submitted *no earlier than fourteen (14) days* before service is to commence, requests for daily service shall be submitted *no earlier than two (2) days* before service is to commence, and requests for hourly service shall be submitted *no earlier than noon the day* before service is to commence. Requests for service received later than *2:00 p.m.* prior to the day service is scheduled to commence will be accommodated if practicable [or such reasonable times that are generally accepted in the region and are consistently adhered to by the Transmission Provider].

18.4 Determination of Available Transmission Capability: Following receipt of a tendered schedule the Transmission Provider will make a determination on a non-discriminatory basis of available transmission capability pursuant to Section 15.2. Such determination shall be made as soon as reasonably practicable after receipt, but not later than the following time periods for the following terms of service *(i) thirty (30) minutes for hourly service, (ii) thirty (30) minutes for daily service, (iii) four (4) hours for weekly service, and (iv) two (2) days for monthly service.* [Or such reasonable times that are generally accepted in the region and are consistently adhered to by the Transmission Provider].

19 *Additional Study Procedures For Firm Point-To-Point Transmission Service Requests*

19.1 Notice of Need for System Impact Study: After receiving a request for service, the Transmission Provider shall determine on a non-discriminatory basis whether a

System Impact Study is needed. A description of the Transmission Provider's methodology for completing a System Impact Study is provided in Attachment D. If the Transmission Provider determines that a System Impact Study is necessary to accommodate the requested service, it shall so inform the Eligible Customer, as soon as practicable. In such cases, the Transmission Provider shall within thirty (30) days of receipt of a Completed Application, tender a System Impact Study Agreement pursuant to which the Eligible Customer shall agree **[30,525]** to reimburse the Transmission Provider for performing the required System Impact Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the System Impact Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the System Impact Study Agreement, its application shall be deemed withdrawn and its deposit, pursuant to Section 17.3, shall be returned with interest.

19.2 System Impact Study Agreement and Cost Reimbursement:

(i) The System Impact Study Agreement will clearly specify the Transmission Provider's estimate of the actual cost, and time for completion of the System Impact Study. The charge shall not exceed the actual cost of the study. In performing the System Impact Study, the Transmission Provider shall rely, to the extent reasonably practicable, on existing transmission planning studies. The Eligible Customer will not be assessed a charge for such existing studies; however, the Eligible Customer will be responsible for charges associated with any modifications to existing planning studies that are reasonably necessary to

evaluate the impact of the Eligible Customer's request for service on the Transmission System.

(ii) If in response to multiple Eligible Customers requesting service in relation to the same competitive solicitation, a single System Impact Study is sufficient for the Transmission Provider to accommodate the requests for service, the costs of that study shall be pro-rated among the Eligible Customers.

(iii) For System Impact Studies that the Transmission Provider conducts on its own behalf, the Transmission Provider shall record the cost of the System Impact Studies pursuant to Section 20.

19.3 System Impact Study Procedures: Upon receipt of an executed System Impact Study Agreement, the Transmission Provider will use due diligence to complete the required System Impact Study within a sixty (60) day period. The System Impact Study shall identify any system constraints and redispatch options, additional Direct Assignment Facilities or Network Upgrades required to provide the requested service. In the event that the Transmission Provider is unable to complete the required System Impact Study within such time period, it shall so notify the Eligible Customer and provide an estimated completion date along with an explanation of the reasons why additional time is required to complete the required studies. A copy of the completed System Impact Study and related work papers shall be made available to the Eligible Customer. The Transmission Provider will use the same due diligence in completing the System Impact Study for an Eligible Customer as it uses when completing studies for itself. The Transmission Provider shall

notify the Eligible Customer immediately upon completion of the System Impact Study if the Transmission System will be adequate to accommodate all or part of a request for service or that no costs are likely to be incurred for new transmission facilities or upgrades. In order for a request to remain a Completed Application, within fifteen (15) days of completion of the System Impact Study the Eligible Customer must execute a Service Agreement or request the filing of an unexecuted Service Agreement pursuant to Section 15.3, or the Application shall be deemed terminated and withdrawn.

19.4 Facilities Study Procedures: If a System Impact Study indicates that additions or upgrades to the Transmission System are needed to supply the Eligible Customer's service request, the Transmission Provider, within thirty (30) days of the completion of the System Impact Study, shall tender to the Eligible Customer a Facilities Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required Facilities Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the Facilities Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the Facilities Study Agreement, its application shall be deemed withdrawn and its deposit, pursuant to Section 17.3, shall be returned **[30,526]** with interest. Upon receipt of an executed Facilities Study Agreement, the Transmission Provider will use due diligence to complete the required Facilities Study within a sixty (60) day period. If the Transmission Provider is unable to complete the Facilities Study in the allotted time period, the Transmission Provider shall notify the Transmission Customer and provide an estimate of the time needed to reach a final determination

along with an explanation of the reasons that additional time is required to complete the study. When completed, the Facilities Study will include a good faith estimate of (i) the cost of Direct Assignment Facilities to be charged to the Transmission Customer, (ii) the Transmission Customer's appropriate share of the cost of any required Network Upgrades as determined pursuant to the provisions of Part II of the Tariff, and (iii) the time required to complete such construction and initiate the requested service. The Transmission Customer shall provide the Transmission Provider with a letter of credit or other reasonable form of security acceptable to the Transmission Provider equivalent to the costs of new facilities or upgrades consistent with commercial practices as established by the Uniform Commercial Code. The Transmission Customer shall have thirty (30) days to execute a Service Agreement or request the filing of an unexecuted Service Agreement and provide the required letter of credit or other form of security or the request will no longer be a Completed Application and shall be deemed terminated and withdrawn.

19.5 Facilities Study Modifications: Any change in design arising from inability to site or construct facilities as proposed will require development of a revised good faith estimate. New good faith estimates also will be required in the event of new statutory or regulatory requirements that are effective before the completion of construction or other circumstances beyond the control of the Transmission Provider that significantly affect the final cost of new facilities or upgrades to be charged to the Transmission Customer pursuant to the provisions of Part II of the Tariff.

19.6 Due Diligence in Completing New Facilities: The Transmission Provider shall use due diligence to add necessary facilities or upgrade its Transmission System within a reasonable time. The Transmission Provider will not upgrade its existing or planned Transmission System in order to provide the requested Firm Point-To-Point Transmission Service if doing so would impair system reliability or otherwise impair or degrade existing firm service.

19.7 Partial Interim Service: If the Transmission Provider determines that it will not have adequate transmission capability to satisfy the full amount of a Completed Application for Firm Point-To-Point Transmission Service, the Transmission Provider nonetheless shall be obligated to offer and provide the portion of the requested Firm Point-To-Point Transmission Service that can be accommodated without addition of any facilities and through redispatch. However, the Transmission Provider shall not be obligated to provide the incremental amount of requested Firm Point-To-Point Transmission Service that requires the addition of facilities or upgrades to the Transmission System until such facilities or upgrades have been placed in service.

19.8 Expedited Procedures for New Facilities: In lieu of the procedures set forth above, the Eligible Customer shall have the option to expedite the process by requesting the Transmission Provider to tender at one time, together with the results of required studies, an "Expedited Service Agreement" pursuant to which the Eligible Customer would agree to compensate the Transmission Provider for all costs incurred pursuant to the terms of the Tariff. In order to exercise this option, the Eligible Customer shall request in writing an expedited Service Agreement covering all of the above-

specified items within thirty (30) days of receiving the results of the System Impact Study identifying needed facility additions or upgrades or costs incurred in providing the requested service. While the Transmission Provider agrees to provide the Eligible Customer with its best estimate of the new facility costs and other charges that may be incurred, such estimate shall not be binding and the Eligible Customer must agree in writing to compensate the Transmission Provider **[30,527]** for all costs incurred pursuant to the provisions of the Tariff. The Eligible Customer shall execute and return such an Expedited Service Agreement within fifteen (15) days of its receipt or the Eligible Customer's request for service will cease to be a Completed Application and will be deemed terminated and withdrawn.

20 Procedures if The Transmission Provider is Unable to Complete New Transmission Facilities for Firm Point-To-Point Transmission Service

20.1 Delays in Construction of New Facilities: If any event occurs that will materially affect the time for completion of new facilities, or the ability to complete them, the Transmission Provider shall promptly notify the Transmission Customer. In such circumstances, the Transmission Provider shall within thirty (30) days of notifying the Transmission Customer of such delays, convene a technical meeting with the Transmission Customer to evaluate the alternatives available to the Transmission Customer. The Transmission Provider also shall make available to the Transmission Customer studies and work papers related to the delay, including all information that is in the possession of the Transmission Provider that is reasonably needed by the Transmission Customer to evaluate any alternatives.

20.2 Alternatives to the Original Facility Additions: When the review process of Section 20.1 determines that one or more alternatives exist to the originally planned construction project, the Transmission Provider shall present such alternatives for consideration by the Transmission Customer. If, upon review of any alternatives, the Transmission Customer desires to maintain its Completed Application subject to construction of the alternative facilities, it may request the Transmission Provider to submit a revised Service Agreement for Firm Point-To-Point Transmission Service. If the alternative approach solely involves Non-Firm Point-To-Point Transmission Service, the Transmission Provider shall promptly tender a Service Agreement for Non-Firm Point-To-Point Transmission Service providing for the service. In the event the Transmission Provider concludes that no reasonable alternative exists and the Transmission Customer disagrees, the Transmission Customer may seek relief under the dispute resolution procedures pursuant to Section 12 or it may refer the dispute to the Commission for resolution.

20.3 Refund Obligation for Unfinished Facility Additions: If the Transmission Provider and the Transmission Customer mutually agree that no other reasonable alternatives exist and the requested service cannot be provided out of existing capability under the conditions of Part II of the Tariff, the obligation to provide the requested Firm Point-To-Point Transmission Service shall terminate and any deposit made by the Transmission Customer shall be returned with interest pursuant to Commission regulations 35.19a(a)(2)(iii). However, the Transmission Customer shall be responsible for all prudently incurred costs by the Transmission Provider through the time construction was suspended.

21 *Provisions Relating to Transmission Construction and Services on the Systems of Other Utilities*

21.1 Responsibility for Third-Party System Additions: The Transmission Provider shall not be responsible for making arrangements for any necessary engineering, permitting, and construction of transmission or distribution facilities on the system(s) of any other entity or for obtaining any regulatory approval for such facilities. The Transmission Provider will undertake reasonable efforts to assist the Transmission Customer in obtaining such arrangements, including without limitation, providing any information or data required by such other electric system pursuant to Good Utility Practice.

21.2 Coordination of Third-Party System Additions: In circumstances where the need for transmission facilities or upgrades is identified pursuant to the provisions of Part II of the Tariff, and if such upgrades further require the addition of transmission facilities on other systems, the Transmission Provider shall have the right to coordinate construction on its own system with the construction required by others. The Transmission Provider, after consultation with the Transmission Customer and representatives of such **[50,528]** other systems, may defer construction of its new transmission facilities, if the new transmission facilities on another system cannot be completed in a timely manner. The Transmission Provider shall notify the Transmission Customer in writing of the basis for any decision to defer construction and the specific problems which must be resolved before it will initiate or resume construction of new facilities. Within sixty (60) days of receiving written notification by the Transmission Provider of its intent to defer construction pursuant to this

section, the Transmission Customer may challenge the decision in accordance with the dispute resolution procedures pursuant to Section 12 or it may refer the dispute to the Commission for resolution.

22 *Changes in Service Specifications*

22.1 Modifications On a Non-Firm Basis: The Transmission Customer taking Firm Point-To-Point Transmission Service may request the Transmission Provider to provide transmission service on a non-firm basis over Receipt and Delivery Points other than those specified in the Service Agreement ("Secondary Receipt and Delivery Points"), in amounts not to exceed its firm capacity reservation, without incurring an additional Non-Firm Point-To-Point Transmission Service charge or executing a new Service Agreement, subject to the following conditions.

(a) Service provided over Secondary Receipt and Delivery Points will be non-firm only, on an as- available basis and will not displace any firm or non-firm service reserved or scheduled by third-parties under the Tariff or by the Transmission Provider on behalf of its Native Load Customers.

(b) The sum of all Firm and non-firm Point-To-Point Transmission Service provided to the Transmission Customer at any time pursuant to this section shall not exceed the Reserved Capacity in the relevant Service Agreement under which such services are provided.

(c) The Transmission Customer shall retain its right to schedule Firm Point-To-Point Transmission Service

at the Receipt and Delivery Points specified in the relevant Service Agreement in the amount of its original capacity reservation.

(d) Service over Secondary Receipt and Delivery Points on a non-firm basis shall not require the filing of an Application for Non-Firm Point-To-Point Transmission Service under the Tariff. However, all other requirements of Part II of the Tariff (except as to transmission rates) shall apply to transmission service on a non-firm basis over Secondary Receipt and Delivery Points.

22.2 Modification On a Firm Basis: Any request by a Transmission Customer to modify Receipt and Delivery Points on a firm basis shall be treated as a new request for service in accordance with Section 17 hereof, except that such Transmission Customer shall not be obligated to pay any additional deposit if the capacity reservation does not exceed the amount reserved in the existing Service Agreement. While such new request is pending, the Transmission Customer shall retain its priority for service at the existing firm Receipt and Delivery Points specified in its Service Agreement.

23 ***Sale or Assignment of Transmission Service***

23.1 Procedures for Assignment or Transfer of Service: Subject to Commission approval of any necessary filings, a Transmission Customer may sell, assign, or transfer all or a portion of its rights under its Service Agreement, but only to another Eligible Customer (the Assignee). The Transmission Customer that sells, assigns or transfers its rights under its Service Agreement is hereafter referred to as the Reseller. Compensation to the Reseller shall not exceed

the higher of (i) the original rate paid by the Reseller, (ii) the Transmission Provider's maximum rate on file at the time of the assignment, or (iii) the Reseller's opportunity cost capped at the Transmission Provider's cost of expansion. If the Assignee does not request any change in the Point(s) of Receipt or the Point(s) of Delivery, or a change in any other term or condition set forth in the original Service Agreement, the Assignee will receive the same services as did the Reseller and the priority of service for the Assignee will be the same as that of the Reseller. A Reseller should notify the Transmission Provider as soon as possible after any assignment or transfer of service **[30,529]** occurs but in any event, notification must be provided prior to any provision of service to the Assignee. The Assignee will be subject to all terms and conditions of this Tariff. If the Assignee requests a change in service, the reservation priority of service will be determined by the Transmission Provider pursuant to Section 13.2.

23.2 Limitations on Assignment or Transfer of Service: If the Assignee requests a change in the Point(s) of Receipt or Point(s) of Delivery, or a change in any other specifications set forth in the original Service Agreement, the Transmission Provider will consent to such change subject to the provisions of the Tariff, provided that the change will not impair the operation and reliability of the Transmission Provider's generation, transmission, or distribution systems. The Assignee shall compensate the Transmission Provider for performing any System Impact Study needed to evaluate the capability of the Transmission System to accommodate the proposed change and any additional costs resulting from such change. The Reseller shall remain liable for the performance of all obligations under the Service Agreement, except as

specifically agreed to by the Parties through an amendment to the Service Agreement.

23.3 Information on Assignment or Transfer of Service: In accordance with Section 4, Resellers may use the Transmission Provider's OASIS to post transmission capacity available for resale.

24 *Metering and Power Factor Correction at Receipt and Delivery Points(s)*

24.1 Transmission Customer Obligations: Unless otherwise agreed, the Transmission Customer shall be responsible for installing and maintaining compatible metering and communications equipment to accurately account for the capacity and energy being transmitted under Part II of the Tariff and to communicate the information to the Transmission Provider. Such equipment shall remain the property of the Transmission Customer.

24.2 Transmission Provider Access to Metering Data: The Transmission Provider shall have access to metering data, which may reasonably be required to facilitate measurements and billing under the Service Agreement.

24.3 Power Factor: Unless otherwise agreed, the Transmission Customer is required to maintain a power factor within the same range as the Transmission Provider pursuant to Good Utility Practices. The power factor requirements are specified in the Service Agreement where applicable.

25 *Compensation for Transmission Service*

Rates for Firm and Non-Firm Point-To-Point Transmission Service are provided in the Schedules appended to the Tariff: Firm Point-To-Point Transmission Service (Schedule 7); and Non-Firm Point-To-Point Transmission Service (Schedule 8). The Transmission Provider shall use Part II of the Tariff to make its Third-Party Sales. The Transmission Provider shall account for such use at the applicable Tariff rates, pursuant to Section 8.

26 *Stranded Cost Recovery*

The Transmission Provider may seek to recover stranded costs from the Transmission Customer pursuant to this Tariff in accordance with the terms, conditions and procedures set forth in FERC Order No. 888. However, the Transmission Provider must separately file any specific proposed stranded cost charge under Section 205 of the Federal Power Act.

27 *Compensation for New Facilities and Redispatch Costs*

Whenever a System Impact Study performed by the Transmission Provider in connection with the provision of Firm Point-To-Point Transmission Service identifies the need for new facilities, the Transmission Customer shall be responsible for such costs to the extent consistent with Commission policy. Whenever a System Impact Study performed by the Transmission Provider identifies capacity constraints that may be relieved more economically by redispatching the Transmission Provider's resources than by building new facilities or upgrading existing facilities to

eliminate such constraints, the Transmission Customer shall be responsible for the redispatch costs to the extent consistent with Commission policy.

III. Network Integration Transmission Service

Preamble

[30,530]

The Transmission Provider will provide Network Integration Transmission Service pursuant to the applicable terms and conditions contained in the Tariff and Service Agreement. Network Integration Transmission Service allows the Network Customer to integrate, economically dispatch and regulate its current and planned Network Resources to serve its Network Load in a manner comparable to that in which the Transmission Provider utilizes its Transmission System to serve its Native Load Customers. Network Integration Transmission Service also may be used by the Network Customer to deliver economy energy purchases to its Network Load from non-designated resources on an as- available basis without additional charge. Transmission service for sales to non-designated loads will be provided pursuant to the applicable terms and conditions of Part II of the Tariff.

28 ***Nature of Network Integration Transmission Service***

28.1 Scope of Service: Network Integration Transmission Service is a transmission service that allows Network Customers to efficiently and economically utilize their Network Resources (as well as other non-designated generation resources) to serve their Network Load located in the Transmission Provider's Control Area and any additional

load that may be designated pursuant to Section 31.3 of the Tariff. The Network Customer taking Network Integration Transmission Service must obtain or provide Ancillary Services pursuant to Section 3.

28.2 Transmission Provider Responsibilities: The Transmission Provider will plan, construct, operate and maintain its Transmission System in accordance with Good Utility Practice in order to provide the Network Customer with Network Integration Transmission Service over the Transmission Provider's Transmission System. The Transmission Provider, on behalf of its Native Load Customers, shall be required to designate resources and loads in the same manner as any Network Customer under Part III of this Tariff. This information must be consistent with the information used by the Transmission Provider to calculate available transmission capability. The Transmission Provider shall include the Network Customer's Network Load in its Transmission System planning and shall, consistent with Good Utility Practice, endeavor to construct and place into service sufficient transmission capacity to deliver the Network Customer's Network Resources to serve its Network Load on a basis comparable to the Transmission Provider's delivery of its own generating and purchased resources to its Native Load Customers.

28.3 Network Integration Transmission Service: The Transmission Provider will provide firm transmission service over its Transmission System to the Network Customer for the delivery of capacity and energy from its designated Network Resources to service its Network Loads on a basis that is comparable to the Transmission Provider's use of the

Transmission System to reliably serve its Native Load Customers.

28.4 Secondary Service: The Network Customer may use the Transmission Provider's Transmission System to deliver energy to its Network Loads from resources that have not been designated as Network Resources. Such energy shall be transmitted, on an as-available basis, at no additional charge. Deliveries from resources other than Network Resources will have a higher priority than any Non-Firm Point-To-Point Transmission Service under Part II of the Tariff.

28.5 Real Power Losses: Real Power Losses are associated with all transmission service. The Transmission Provider is not obligated to provide Real Power Losses. The Network Customer is responsible for replacing losses associated with all transmission service as calculated by the Transmission Provider. The applicable Real Power Loss factors are as follows: [To be completed by the Transmission Provider].

28.6 Restrictions on Use of Service: The Network Customer shall not use Network Integration Transmission Service for (i) sales of capacity and energy to non-designated loads, or (ii) direct or indirect provision of transmission service by the Network Customer to third parties. All Network Customers taking Network Integration Transmission Service shall use Point-To-Point Transmission Service under Part II of the Tariff for any Third-Party Sale which requires **[30,531]** use of the Transmission Provider's Transmission System.

29 *Initiating Service*

29.1 Condition Precedent for Receiving Service: Subject to the terms and conditions of Part III of the Tariff, the Transmission Provider will provide Network Integration Transmission Service to any Eligible Customer, provided that (i) the Eligible Customer completes an Application for service as provided under Part III of the Tariff, (ii) the Eligible Customer and the Transmission Provider complete the technical arrangements set forth in Sections 29.3 and 29.4, (iii) the Eligible Customer executes a Service Agreement pursuant to Attachment F for service under Part III of the Tariff or requests in writing that the Transmission Provider file a proposed unexecuted Service Agreement with the Commission, and (iv) the Eligible Customer executes a Network Operating Agreement with the Transmission Provider pursuant to Attachment G.

29.2 Application Procedures: An Eligible Customer requesting service under Part III of the Tariff must submit an Application, with a deposit approximating the charge for one month of service, to the Transmission Provider as far as possible in advance of the month in which service is to commence. Unless subject to the procedures in Section 2, Completed Applications for Network Integration Transmission Service will be assigned a priority according to the date and time the Application is received, with the earliest Application receiving the highest priority. Applications should be submitted by entering the information listed below on the Transmission Provider's OASIS. Prior to implementation of the Transmission Provider's OASIS, a Completed Application may be submitted by (i) transmitting the required information to the Transmission Provider by telefax, or (ii) providing the

information by telephone over the Transmission Provider's time recorded telephone line. Each of these methods will provide a time-stamped record for establishing the service priority of the Application. A Completed Application shall provide all of the information included in 18 CFR §2.20 including but not limited to the following:

(i) The identity, address, telephone number and facsimile number of the party requesting service;

(ii) A statement that the party requesting service is, or will be upon commencement of service, an Eligible Customer under the Tariff;

(iii) A description of the Network Load at each delivery point. This description should separately identify and provide the Eligible Customer's best estimate of the total loads to be served at each transmission voltage level, and the loads to be served from each Transmission Provider substation at the same transmission voltage level. The description should include a ten (10) year forecast of summer and winter load and resource requirements beginning with the first year after the service is scheduled to commence;

(iv) The amount and location of any interruptible loads included in the Network Load. This shall include the summer and winter capacity requirements for each interruptible load (had such load not been interruptible), that portion of the load subject to interruption, the conditions under which an interruption can be implemented and any limitations on the amount and frequency of interruptions. An Eligible Customer should identify the amount of interruptible

customer load (if any) included in the 10 year load forecast provided in response to (iii) above;

(v) A description of Network Resources (current and 10-year projection), which shall include, for each Network Resource:

- Unit size and amount of capacity from that unit to be designated as Network Resource

- VAR capability (both leading and lagging) of all generators

- Operating restrictions

- Any periods of restricted operations throughout the year

- Maintenance schedules

- Minimum loading level of unit - Normal operating level of unit

- Any must-run unit designations required for system reliability or contract reasons

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- Approximate variable generating cost ($/MWH) for redispatch computations

- Arrangements governing sale and delivery of power to third parties from generating facilities located in the

Transmission Provider Control Area, where only a portion of unit output is designated as a Network Resource

- Description of purchased power designated as a Network Resource including source of supply, Control Area location, transmission arrangements and delivery point(s) to the Transmission Provider's Transmission System;

(vi) Description of Eligible Customer's transmission system:

- Load flow and stability data, such as real and reactive parts of the load, lines, transformers, reactive devices and load type, including normal and emergency ratings of all transmission equipment in a load flow format compatible with that used by the Transmission Provider

- Operating restrictions needed for reliability

- Operating guides employed by system operators

- Contractual restrictions or committed uses of the Eligible Customer's transmission system, other than the Eligible Customer's Network Loads and Resources

- Location of Network Resources described in subsection (v) above

- 10 year projection of system expansions or upgrades

- Transmission System maps that include any proposed expansions or upgrades

- Thermal ratings of Eligible Customer's Control Area ties with other Control Areas; and

(vii) Service Commencement Date and the term of the requested Network Integration Transmission Service. The minimum term for Network Integration Transmission Service is one year.

Unless the Parties agree to a different time frame, the Transmission Provider must acknowledge the request within ten (10) days of receipt. The acknowledgement must include a date by which a response, including a Service Agreement, will be sent to the Eligible Customer. If an Application fails to meet the requirements of this section, the Transmission Provider shall notify the Eligible Customer requesting service within fifteen (15) days of receipt and specify the reasons for such failure. Wherever possible, the Transmission Provider will attempt to remedy deficiencies in the Application through informal communications with the Eligible Customer. If such efforts are unsuccessful, the Transmission Provider shall return the Application without prejudice to the Eligible Customer filing a new or revised Application that fully complies with the requirements of this section. The Eligible Customer will be assigned a new priority consistent with the date of the new or revised Application. The Transmission Provider shall treat this information consistent with the standards of conduct contained in Part 37 of the Commission's regulations.

29.3 Technical Arrangements to be Completed Prior to Commencement of Service: Network Integration Transmission Service shall not commence until the Transmission Provider and the Network Customer, or a third party, have completed installation of all equipment specified under the Network Operating Agreement consistent with Good Utility Practice and any additional requirements reasonably and consistently imposed to ensure the reliable operation of the Transmission System. The Transmission Provider shall exercise reasonable efforts, in coordination with the Network Customer, to complete such arrangements as soon as practicable taking into consideration the Service Commencement Date.

29.4 Network Customer Facilities: The provision of Network Integration Transmission Service shall be conditioned upon the Network Customer's constructing, maintaining and operating the facilities on its side of each delivery point or interconnection necessary to reliably deliver capacity and energy from the Transmission Provider's Transmission System to the Network Customer. The Network Customer shall be solely responsible for constructing or installing all facilities on the Network Customer's side of each such delivery point or interconnection.

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29.5 Filing of Service Agreement: The Transmission Provider will file Service Agreements with the Commission in compliance with applicable Commission regulations.

30 *Network Resources*

30.1 Designation of Network Resources: Network Resources shall include all generation owned, purchased or leased by the Network Customer designated to serve Network Load under the Tariff. Network Resources may not include resources, or any portion thereof, that are committed for sale to non-designated third party load or otherwise cannot be called upon to meet the Network Customer's Network Load on a non-interruptible basis. Any owned or purchased resources that were serving the Network Customer's loads under firm agreements entered into on or before the Service Commencement Date shall initially be designated as Network Resources until the Network Customer terminates the designation of such resources.

30.2 Designation of New Network Resources: The Network Customer may designate a new Network Resource by providing the Transmission Provider with as much advance notice as practicable. A designation of a new Network Resource must be made by a request for modification of service pursuant to an Application under Section 29.

30.3 Termination of Network Resources: The Network Customer may terminate the designation of all or part of a generating resource as a Network Resource at any time but should provide notification to the Transmission Provider as soon as reasonably practicable.

30.4 Operation of Network Resources: The Network Customer shall not operate its designated Network Resources located in the Network Customer's or Transmission Provider's Control Area such that the output of those facilities

exceeds its designated Network Load, plus non-firm sales delivered pursuant to Part II of the Tariff, plus losses. This limitation shall not apply to changes in the operation of a Transmission Customer's Network Resources at the request of the Transmission Provider to respond to an emergency or other unforeseen condition which may impair or degrade the reliability of the Transmission System.

30.5 Network Customer Redispatch Obligation: As a condition to receiving Network Integration Transmission Service, the Network Customer agrees to redispatch its Network Resources as requested by the Transmission Provider pursuant to Section 33.2. To the extent practical, the redispatch of resources pursuant to this section shall be on a least cost, non-discriminatory basis between all Network Customers, and the Transmission Provider.

30.6 Transmission Arrangements for Network Resources Not Physically Interconnected With The Transmission Provider: The Network Customer shall be responsible for any arrangements necessary to deliver capacity and energy from a Network Resource not physically interconnected with the Transmission Provider's Transmission System. The Transmission Provider will undertake reasonable efforts to assist the Network Customer in obtaining such arrangements, including without limitation, providing any information or data required by such other entity pursuant to Good Utility Practice.

30.7 Limitation on Designation of Network Resources: The Network Customer must demonstrate that it owns or has committed to purchase generation pursuant to an executed contract in order to designate a generating resource

as a Network Resource. Alternatively, the Network Customer may establish that execution of a contract is contingent upon the availability of transmission service under Part III of the Tariff.

30.8 Use of Interface Capacity by the Network Customer: There is no limitation upon a Network Customer's use of the Transmission Provider's Transmission System at any particular interface to integrate the Network Customer's Network Resources (or substitute economy purchases) with its Network Loads. However, a Network Customer's use of the Transmission Provider's total interface capacity with other transmission systems may not exceed the Network Customer's Load.

30.9 Network Customer Owned Transmission Facilities: The Network **[30,534]** Customer that owns existing transmission facilities that are integrated with the Transmission Provider's Transmission System may be eligible to receive consideration either through a billing credit or some other mechanism. In order to receive such consideration the Network Customer must demonstrate that its transmission facilities are integrated into the plans or operations of the Transmission Provider to serve its power and transmission customers. For facilities constructed by the Network Customer subsequent to the Service Commencement Date under Part III of the Tariff, the Network Customer shall receive credit where such facilities are jointly planned and installed in coordination with the Transmission Provider. Calculation of the credit shall be addressed in either the Network Customer's Service Agreement or any other agreement between the Parties.

31 *Designation of Network Load*

31.1 Network Load: The Network Customer must designate the individual Network Loads on whose behalf the Transmission Provider will provide Network Integration Transmission Service. The Network Loads shall be specified in the Service Agreement.

31.2 New Network Loads Connected With the Transmission Provider: The Network Customer shall provide the Transmission Provider with as much advance notice as reasonably practicable of the designation of new Network Load that will be added to its Transmission System. A designation of new Network Load must be made through a modification of service pursuant to a new Application. The Transmission Provider will use due diligence to install any transmission facilities required to interconnect a new Network Load designated by the Network Customer. The costs of new facilities required to interconnect a new Network Load shall be determined in accordance with the procedures provided in Section 32.4 and shall be charged to the Network Customer in accordance with Commission policies.

31.3 Network Load Not Physically Interconnected with the Transmission Provider: This section applies to both initial designation pursuant to Section 31.1 and the subsequent addition of new Network Load not physically interconnected with the Transmission Provider. To the extent that the Network Customer desires to obtain transmission service for a load outside the Transmission Provider's Transmission System, the Network Customer shall have the option of (1) electing to include the entire load as Network Load for all purposes under Part III of the Tariff and designating Network

Resources in connection with such additional Network Load, or (2) excluding that entire load from its Network Load and purchasing Point-To-Point Transmission Service under Part II of the Tariff. To the extent that the Network Customer gives notice of its intent to add a new Network Load as part of its Network Load pursuant to this section the request must be made through a modification of service pursuant to a new Application.

31.4 New Interconnection Points: To the extent the Network Customer desires to add a new Delivery Point or interconnection point between the Transmission Provider's Transmission System and a Network Load, the Network Customer shall provide the Transmission Provider with as much advance notice as reasonably practicable.

31.5 Changes in Service Requests: Under no circumstances shall the Network Customer's decision to cancel or delay a requested change in Network Integration Transmission Service (*e.g.* the addition of a new Network Resource or designation of a new Network Load) in any way relieve the Network Customer of its obligation to pay the costs of transmission facilities constructed by the Transmission Provider and charged to the Network Customer as reflected in the Service Agreement. However, the Transmission Provider must treat any requested change in Network Integration Transmission Service in a non-discriminatory manner.

31.6 Annual Load and Resource Information Updates: The Network Customer shall provide the Transmission Provider with annual updates of Network Load and Network Resource forecasts consistent with those

included in its Application for Network Integration Transmission Service under Part III of the Tariff. The Network Customer **[30,535]** also shall provide the Transmission Provider with timely written notice of material changes in any other information provided in its Application relating to the Network Customer's Network Load, Network Resources, its transmission system or other aspects of its facilities or operations affecting the Transmission Provider's ability to provide reliable service.

32 *Additional Study Procedures For Network Integration Transmission Service Requests*

32.1 Notice of Need for System Impact Study: After receiving a request for service, the Transmission Provider shall determine on a non-discriminatory basis whether a System Impact Study is needed. A description of the Transmission Provider's methodology for completing a System Impact Study is provided in Attachment D. If the Transmission Provider determines that a System Impact Study is necessary to accommodate the requested service, it shall so inform the Eligible Customer, as soon as practicable. In such cases, the Transmission Provider shall within thirty (30) days of receipt of a Completed Application, tender a System Impact Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required System Impact Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the System Impact Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the System Impact Study Agreement, its Application shall be deemed withdrawn and its deposit shall be returned with interest.

32.2 System Impact Study Agreement and Cost Reimbursement:

(i) The System Impact Study Agreement will clearly specify the Transmission Provider's estimate of the actual cost, and time for completion of the System Impact Study. The charge shall not exceed the actual cost of the study. In performing the System Impact Study, the Transmission Provider shall rely, to the extent reasonably practicable, on existing transmission planning studies. The Eligible Customer will not be assessed a charge for such existing studies; however, the Eligible Customer will be responsible for charges associated with any modifications to existing planning studies that are reasonably necessary to evaluate the impact of the Eligible Customer's request for service on the Transmission System.

(ii) If in response to multiple Eligible Customers requesting service in relation to the same competitive solicitation, a single System Impact Study is sufficient for the Transmission Provider to accommodate the service requests, the costs of that study shall be pro-rated among the Eligible Customers.

(iii) For System Impact Studies that the Transmission Provider conducts on its own behalf, the Transmission Provider shall record the cost of the System Impact Studies pursuant to Section 8.

32.3 System Impact Study Procedures: Upon receipt of an executed System Impact Study Agreement, the Transmission Provider will use due diligence to complete the required System Impact Study within a sixty (60) day period.

The System Impact Study shall identify any system constraints and redispatch options, additional Direct Assignment Facilities or Network Upgrades required to provide the requested service. In the event that the Transmission Provider is unable to complete the required System Impact Study within such time period, it shall so notify the Eligible Customer and provide an estimated completion date along with an explanation of the reasons why additional time is required to complete the required studies. A copy of the completed System Impact Study and related work papers shall be made available to the Eligible Customer. The Transmission Provider will use the same due diligence in completing the System Impact Study for an Eligible Customer as it uses when completing studies for itself. The Transmission Provider shall notify the Eligible Customer immediately upon completion of the System Impact Study if the Transmission System will be adequate to accommodate all or part of a request for service or that no costs are likely to be incurred for new transmission facilities or upgrades. In order for a request to **[30,536]** remain a Completed Application, within fifteen (15) days of completion of the System Impact Study the Eligible Customer must execute a Service Agreement or request the filing of an unexecuted Service Agreement, or the Application shall be deemed terminated and withdrawn.

32.4 Facilities Study Procedures: If a System Impact Study indicates that additions or upgrades to the Transmission System are needed to supply the Eligible Customer's service request, the Transmission Provider, within thirty (30) days of the completion of the System Impact Study, shall tender to the Eligible Customer a Facilities Study Agreement pursuant to which the Eligible Customer shall agree to reimburse the Transmission Provider for performing the required Facilities

Study. For a service request to remain a Completed Application, the Eligible Customer shall execute the Facilities Study Agreement and return it to the Transmission Provider within fifteen (15) days. If the Eligible Customer elects not to execute the Facilities Study Agreement, its Application shall be deemed withdrawn and its deposit shall be returned with interest. Upon receipt of an executed Facilities Study Agreement, the Transmission Provider will use due diligence to complete the required Facilities Study within a sixty (60) day period. If the Transmission Provider is unable to complete the Facilities Study in the allotted time period, the Transmission Provider shall notify the Eligible Customer and provide an estimate of the time needed to reach a final determination along with an explanation of the reasons that additional time is required to complete the study. When completed, the Facilities Study will include a good faith estimate of (i) the cost of Direct Assignment Facilities to be charged to the Eligible Customer, (ii) the Eligible Customer's appropriate share of the cost of any required Network Upgrades, and (iii) the time required to complete such construction and initiate the requested service. The Eligible Customer shall provide the Transmission Provider with a letter of credit or other reasonable form of security acceptable to the Transmission Provider equivalent to the costs of new facilities or upgrades consistent with commercial practices as established by the Uniform Commercial Code. The Eligible Customer shall have thirty (30) days to execute a Service Agreement or request the filing of an unexecuted Service Agreement and provide the required letter of credit or other form of security or the request no longer will be a Completed Application and shall be deemed terminated and withdrawn.

33 *Load Shedding and Curtailments*

33.1 Procedures: Prior to the Service Commencement Date, the Transmission Provider and the Network Customer shall establish Load Shedding and Curtailment procedures pursuant to the Network Operating Agreement with the objective of responding to contingencies on the Transmission System. The Parties will implement such programs during any period when the Transmission Provider determines that a system contingency exists and such procedures are necessary to alleviate such contingency. The Transmission Provider will notify all affected Network Customers in a timely manner of any scheduled Curtailment.

33.2 Transmission Constraints: During any period when the Transmission Provider determines that a transmission constraint exists on the Transmission System, and such constraint may impair the reliability of the Transmission Provider's system, the Transmission Provider will take whatever actions, consistent with Good Utility Practice, that are reasonably necessary to maintain the reliability of the Transmission Provider's system. To the extent the Transmission Provider determines that the reliability of the Transmission System can be maintained by redispatching resources, the Transmission Provider will initiate procedures pursuant to the Network Operating Agreement to redispatch all Network Resources and the Transmission Provider's own resources on a least-cost basis without regard to the ownership of such resources. Any redispatch under this section may not unduly discriminate between the Transmission Provider's use of the Transmission System on behalf of its Native Load Customers and any

Network Customer's use of the Transmission System to serve its designated Network Load.

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33.3 Cost Responsibility for Relieving Transmission Constraints: Whenever the Transmission Provider implements least-cost redispatch procedures in response to a transmission constraint, the Transmission Provider and Network Customers will each bear a proportionate share of the total redispatch cost based on their respective Load Ratio Shares.

33.4 Curtailments of Scheduled Deliveries: If a transmission constraint on the Transmission Provider's Transmission System cannot be relieved through the implementation of least-cost redispatch procedures and the Transmission Provider determines that it is necessary to Curtail scheduled deliveries, the Parties shall Curtail such schedules in accordance with the Network Operating Agreement.

33.5 Allocation of Curtailments: The Transmission Provider shall, on a non-discriminatory basis, Curtail the transaction(s) that effectively relieve the constraint. However, to the extent practicable and consistent with Good Utility Practice, any Curtailment will be shared by the Transmission Provider and Network Customer in proportion to their respective Load Ratio Shares. The Transmission Provider shall not direct the Network Customer to Curtail schedules to an extent greater than the Transmission Provider would Curtail the Transmission Provider's schedules under similar circumstances.

33.6 Load Shedding: To the extent that a system contingency exists on the Transmission Provider's Transmission System and the Transmission Provider determines that it is necessary for the Transmission Provider and the Network Customer to shed load, the Parties shall shed load in accordance with previously established procedures under the Network Operating Agreement.

33.7 System Reliability: Notwithstanding any other provisions of this Tariff, the Transmission Provider reserves the right, consistent with Good Utility Practice and on a not unduly discriminatory basis, to Curtail Network Integration Transmission Service without liability on the Transmission Provider's part for the purpose of making necessary adjustments to, changes in, or repairs on its lines, substations and facilities, and in cases where the continuance of Network Integration Transmission Service would endanger persons or property. In the event of any adverse condition(s) or disturbance(s) on the Transmission Provider's Transmission System or on any other system(s) directly or indirectly interconnected with the Transmission Provider's Transmission System, the Transmission Provider, consistent with Good Utility Practice, also may Curtail Network Integration Transmission Service in order to (i) limit the extent or damage of the adverse condition(s) or disturbance(s), (ii) prevent damage to generating or transmission facilities, or (iii) expedite restoration of service. The Transmission Provider will give the Network Customer as much advance notice as is practicable in the event of such Curtailment. Any Curtailment of Network Integration Transmission Service will be not unduly discriminatory relative to the Transmission Provider's use of the Transmission System on behalf of its Native Load Customers. The Transmission Provider shall specify the rate

treatment and all related terms and conditions applicable in the event that the Network Customer fails to respond to established Load Shedding and Curtailment procedures.

34 *Rates and Charges*

The Network Customer shall pay the Transmission Provider for any Direct Assignment Facilities, Ancillary Services, and applicable study costs, consistent with Commission policy, along with the following:

34.1 Monthly Demand Charge: The Network Customer shall pay a monthly Demand Charge, which shall be determined by multiplying its Load Ratio Share times one twelfth (1/12) of the Transmission Provider's Annual Transmission Revenue Requirement specified in Schedule H.

34.2 Determination of Network Customer's Monthly Network Load: The Network Customer's monthly Network Load is its hourly load (including its designated Network Load not physically interconnected with the Transmission Provider under Section 31.3) coincident with the Transmission Provider's Monthly Transmission System Peak.

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34.3 Determination of Transmission Provider's Monthly Transmission System Load: The Transmission Provider's monthly Transmission System load is the Transmission Provider's Monthly Transmission System Peak minus the coincident peak usage of all Firm Point-To-Point Transmission Service customers pursuant to Part II of this Tariff plus the Reserved Capacity of all Firm Point-To-Point Transmission Service customers.

34.4 Redispatch Charge: The Network Customer shall pay a Load Ratio Share of any redispatch costs allocated between the Network Customer and the Transmission Provider pursuant to Section 33. To the extent that the Transmission Provider incurs an obligation to the Network Customer for redispatch costs in accordance with Section 33, such amounts shall be credited against the Network Customer's bill for the applicable month.

34.5 Stranded Cost Recovery: The Transmission Provider may seek to recover stranded costs from the Network Customer pursuant to this Tariff in accordance with the terms, conditions and procedures set forth in FERC Order No. 888. However, the Transmission Provider must separately file any proposal to recover stranded costs under Section 205 of the Federal Power Act.

35 ***Operating Arrangements***

35.1 Operation under The Network Operating Agreement: The Network Customer shall plan, construct, operate and maintain its facilities in accordance with Good Utility Practice and in conformance with the Network Operating Agreement.

35.2 Network Operating Agreement: The terms and conditions under which the Network Customer shall operate its facilities and the technical and operational matters associated with the implementation of Part III of the Tariff shall be specified in the Network Operating Agreement. The Network Operating Agreement shall provide for the Parties to (i) operate and maintain equipment necessary for integrating the Network Customer within the Transmission Provider's

Transmission System (including, but not limited to, remote terminal units, metering, communications equipment and relaying equipment), (ii) transfer data between the Transmission Provider and the Network Customer (including, but not limited to, heat rates and operational characteristics of Network Resources, generation schedules for units outside the Transmission Provider's Transmission System, interchange schedules, unit outputs for redispatch required under Section 33, voltage schedules, loss factors and other real time data), (iii) use software programs required for data links and constraint dispatching, (iv) exchange data on forecasted loads and resources necessary for long-term planning, and (v) address any other technical and operational considerations required for implementation of Part III of the Tariff, including scheduling protocols. The Network Operating Agreement will recognize that the Network Customer shall either (i) operate as a Control Area under applicable guidelines of the North American Electric Reliability Council (NERC) and the [applicable regional reliability council], (ii) satisfy its Control Area requirements, including all necessary Ancillary Services, by contracting with the Transmission Provider, or (iii) satisfy its Control Area requirements, including all necessary Ancillary Services, by contracting with another entity, consistent with Good Utility Practice, which satisfies NERC and the [applicable regional reliability council] requirements. The Transmission Provider shall not unreasonably refuse to accept contractual arrangements with another entity for Ancillary Services. The Network Operating Agreement is included in Attachment G.

35.3 Network Operating Committee: A Network Operating Committee (Committee) shall be established to coordinate operating criteria for the Parties' respective

responsibilities under the Network Operating Agreement. Each Network Customer shall be entitled to have at least one representative on the Committee. The Committee shall meet from time to time as need requires, but no less than once each calendar year.

Schedule 1--Scheduling, System Control and Dispatch Service

This service is required to schedule the movement of power through, out of, **[30,539]** within, or into a Control Area. This service can be provided only by the operator of the Control Area in which the transmission facilities used for transmission service are located. Scheduling, System Control and Dispatch Service is to be provided directly by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for Scheduling, System Control and Dispatch Service are to be based on the rates set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 2--Reactive Supply and Voltage Control from Generation Sources Service

In order to maintain transmission voltages on the Transmission Provider's transmission facilities within acceptable limits, generation facilities under the control of the control area operator are operated to produce (or absorb) reactive power. Thus, Reactive Supply and Voltage Control from Generation Sources Service must be provided for each transaction on the Transmission Provider's transmission facilities. The amount of Reactive Supply and Voltage Control from Generation Sources Service that must be supplied with respect to the Transmission Customer's transaction will be determined based on the reactive power support necessary to maintain transmission voltages within limits that are generally accepted in the region and consistently adhered to by the Transmission Provider.

Reactive Supply and Voltage Control from Generation Sources Service is to be provided directly by the Transmission Provider (if the Transmission Provider is the Control Area operator) or indirectly by the Transmission Provider making arrangements with the Control Area operator that performs this service for the Transmission Provider's Transmission System. The Transmission Customer must purchase this service from the Transmission Provider or the Control Area operator. The charges for such service will be based on the rates set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by the Control Area operator.

Schedule 3--Regulation and Frequency Response Service

Regulation and Frequency Response Service is necessary to provide for the continuous balancing of resources (generation and interchange) with load and for maintaining scheduled Interconnection frequency at sixty cycles per second (60 Hz). Regulation and Frequency Response Service is accomplished by committing on-line generation whose output is raised or lowered (predominantly through the use of automatic generating control equipment) as necessary to follow the moment-by-moment changes in load. The obligation to maintain this balance between resources and load lies with the Transmission Provider (or the Control Area operator that performs this function for the Transmission Provider). The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Regulation and Frequency Response Service obligation. The amount of and charges for Regulation and Frequency Response Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 4--Energy Imbalance Service

Energy Imbalance Service is provided when a difference occurs between the scheduled and the actual delivery of energy to a load located within a Control Area over a single hour. The Transmission Provider must offer this

service when the **[30,540]** transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Energy Imbalance Service obligation. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

The Transmission Provider shall establish a deviation band of +/- 1.5 percent (with a minimum of 2 MW) of the scheduled transaction to be applied hourly to any energy imbalance that occurs as a result of the Transmission Customer's scheduled transaction(s). Parties should attempt to eliminate energy imbalances within the limits of the deviation band within thirty (30) days or within such other reasonable period of time as is generally accepted in the region and consistently adhered to by the Transmission Provider. If an energy imbalance is not corrected within thirty (30) days or a reasonable period of time that is generally accepted in the region and consistently adhered to by the Transmission Provider, the Transmission Customer will compensate the Transmission Provider for such service. Energy imbalances outside the deviation band will be subject to charges to be specified by the Transmission Provider. The charges for Energy Imbalance Service are set forth below.

Schedule 5--Operating Reserve - Spinning Reserve Service

Spinning Reserve Service is needed to serve load immediately in the event of a system contingency. Spinning

Reserve Service may be provided by generating units that are on-line and loaded at less than maximum output. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Spinning Reserve Service obligation. The amount of and charges for Spinning Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 6--Operating Reserve - Supplemental Reserve Service

Supplemental Reserve Service is needed to serve load in the event of a system contingency; however, it is not available immediately to serve load but rather within a short period of time. Supplemental Reserve Service may be provided by generating units that are on-line but unloaded, by quick-start generation or by interruptible load. The Transmission Provider must offer this service when the transmission service is used to serve load within its Control Area. The Transmission Customer must either purchase this service from the Transmission Provider or make alternative comparable arrangements to satisfy its Supplemental Reserve Service obligation. The amount of and charges for Supplemental Reserve Service are set forth below. To the extent the Control Area operator performs this service for the Transmission Provider, charges to the Transmission Customer

are to reflect only a pass-through of the costs charged to the Transmission Provider by that Control Area operator.

Schedule 7 Long-Term Firm and Short-Term Firm Point-To-Point Transmission Service

The Transmission Customer shall compensate the Transmission Provider each month for Reserved Capacity at the sum of the applicable charges set forth below:

1) Yearly delivery: one-twelfth of the demand charge of $---/KW of Reserved Capacity per year.

2) Monthly delivery: $---/KW of Reserved Capacity per month.

3) Weekly delivery: $---/KW of Reserved Capacity per week.

4) Daily delivery: $---/KW of Reserved Capacity per day.

The total demand charge in any week, pursuant to a reservation for Daily delivery, shall not exceed the rate specified in section (3) above times the highest amount in kilowatts of Reserved Capacity in any day during such week.

5) Discounts: Three principal requirements apply to discounts for transmission service as follows (1) any offer of a discount **[30,541]** made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts (including requests for use by one's wholesale merchant or an

affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. For any discount agreed upon for service on a path, from point(s) of receipt to point(s) of delivery, the Transmission Provider must offer the same discounted transmission service rate for the same time period to all Eligible Customers on all unconstrained transmission paths that go to the same point(s) of delivery on the Transmission System.

Schedule 8--Non-Firm Point-To-Point Transmission Service

The Transmission Customer shall compensate the Transmission Provider for Non-Firm Point-To-Point Transmission Service up to the sum of the applicable charges set forth below:

1) Monthly delivery: $---/KW of Reserved Capacity per month.

2) Weekly delivery: $---/KW of Reserved Capacity per week.

3) Daily delivery: $---/KW of Reserved Capacity per day.

The total demand charge in any week, pursuant to a reservation for Daily delivery, shall not exceed the rate specified in section (2) above times the highest amount in kilowatts of Reserved Capacity in any day during such week.

4) Hourly delivery: The basic charge shall be that agreed upon by the Parties at the time this service is reserved and in no event shall exceed $---/MWH. The total demand charge in any day, pursuant to a reservation for Hourly delivery, shall not exceed the rate specified in section (3) above times the highest amount in kilowatts of Reserved Capacity in any hour during such day. In addition, the total demand charge in any week, pursuant to a reservation for Hourly or Daily delivery, shall not exceed the rate specified in section (2) above times the highest amount in kilowatts of Reserved Capacity in any hour during such week.

5) Discounts: Three principal requirements apply to discounts for transmission service as follows (1) any offer of a discount made by the Transmission Provider must be announced to all Eligible Customers solely by posting on the OASIS, (2) any customer-initiated requests for discounts (including requests for use by one's wholesale merchant or an affiliate's use) must occur solely by posting on the OASIS, and (3) once a discount is negotiated, details must be immediately posted on the OASIS. For any discount agreed upon for service on a path, from point(s) of receipt to point(s) of delivery, the Transmission Provider must offer the same discounted transmission service rate for the same time period to all Eligible Customers on all unconstrained transmission paths that go to the same point(s) of delivery on the Transmission System.

Attachment A--Form Of Service Agreement For Firm Point-To-Point Transmission Service

1.0 This Service Agreement, dated as of _____, is entered into, by and between

_____ (the Transmission Provider), and _____ ("Transmission Customer").

2.0 The Transmission Customer has been determined by the Transmission Provider to have a Completed Application for Firm Point-To-Point Transmission Service under the Tariff.

3.0 The Transmission Customer has provided to the Transmission Provider an Application deposit in accordance with the provisions of Section 17.3 of the Tariff.

4.0 Service under this agreement shall commence on the later of (l) the requested service commencement date, or (2) the date on which construction of any Direct Assignment Facilities and/or Network Upgrades are completed, or (3) such other date as it is permitted to become effective by the Commission. Service under this agreement shall terminate on such date as mutually agreed upon by the parties.

5.0 The Transmission Provider agrees to provide and the Transmission Customer agrees to take and pay for Firm Point-To-Point Transmission Service in accordance with the provisions of Part II of the Tariff and this Service Agreement.

6.0 Any notice or request made to or by either Party regarding this Service Agreement shall be made to the representative of the other Party as indicated below.

[30,542]
Transmission Provider:

_____

_____

Transmission Customer:

_____

_____

_____

7.0 The Tariff is incorporated herein and made a part hereof.

IN WITNESS WHEREOF, the Parties have caused this Service Agreement to be executed by their respective authorized officials.

Transmission Provider:

By:
Name _____
Title _____
Date _____

Transmission Customer:

By:
Name _____
Title _____
Date _____

Specifications For Long-Term Firm Point-To-Point Transmission Service

1.0 Term of Transaction: _____
Start Date: _____
Termination Date: _____

2.0 Description of capacity and energy to be transmitted by Transmission Provider including the electric Control Area in which the transaction originates.

_____

3.0 Point(s) of Receipt: _____
Delivering Party: _____

4.0 Point(s) of Delivery: _____
Receiving Party: _____

5.0 Maximum amount of capacity and energy to be transmitted (Reserved Capacity): _____

6.0 Designation of party(ies) subject to reciprocal service obligation: _____

7.0 Name(s) of any Intervening Systems providing transmission service: _____

8.0 Service under this Agreement may be subject to some combination of the charges detailed below. (The appropriate charges for individual transactions will be determined in accordance with the terms and conditions of the Tariff.)

8.1 Transmission Charge: _____

8.2 System Impact and/or Facilities Study Charge(s):

_____

8.3 Direct Assignment Facilities Charge:

_____

_____

8.4 Ancillary Services Charges:

_____

_____

_____

_____

_____

_____

Attachment B--Form Of Service Agreement For Non-Firm Point-To-Point Transmission Service

1.0 This Service Agreement, dated as of _____, is entered into, by and between _____ (the Transmission Provider), and _____ (Transmission Customer).

2.0 The Transmission Customer has been determined by the Transmission Provider to be a Transmission Customer under Part II of the Tariff and has filed a Completed Application for Non-Firm Point-To-Point Transmission Service in accordance with Section 18.2 of the Tariff.

3.0 Service under this Agreement shall be provided by the Transmission Provider upon request by an authorized representative of the Transmission Customer.

4.0 The Transmission Customer agrees to supply information the Transmission Provider deems reasonably

necessary in accordance with Good Utility Practice in order for it to provide the requested service.

5.0 The Transmission Provider agrees to provide and the Transmission Customer agrees to take and pay for Non-Firm Point-To-Point Transmission Service in accordance with the provisions of Part II of the Tariff and this Service Agreement.

[30,543]

6.0 Any notice or request made to or by either Party regarding this Service Agreement shall be made to the representative of the other Party as indicated below.

Transmission Provider:

_____

_____

Transmission Customer:

_____

_____

7.0 The Tariff is incorporated herein and made a part hereof. IN WITNESS WHEREOF, the Parties have caused this Service Agreement to be executed by their respective authorized officials.

Transmission Provider:

By:
Name _____
Title _____
Date _____

Transmission Customer:

By:
Name _____
Title _____
Date _____

Attachment C--Methodology To Assess Available Transmission Capability

To be filed by the Transmission Provider

Attachment D--Methodology for Completing a System Impact Study

To be filed by the Transmission Provider

Attachment E--Index Of Point-To-Point Transmission Service Customers

_____
Customer
Date of Customer Service Agreement

_____

Attachment F--Service Agreement For Network Integration Transmission Service

To be filed by the Transmission Provider

Attachment G--Network Operating Agreement

To be filed by the Transmission Provider

Attachment H--Annual Transmission Revenue Requirement For Network Integration Transmission Service

1. The Annual Transmission Revenue Requirement for purposes of the Network Integration Transmission Service shall be _____ .

2. The amount in (1) shall be effective until amended by the Transmission Provider or modified by the Commission.

Attachment I--Index Of Network Integration Transmission Service Customers

_____

Customer
Date of Customer Service Agreement

_____

In The United States Court of Appeals
For The District of Columbia Circuit

COMPLEX
No. 97-1715

SEPTEMBER TERM, 1997

Transmission Access Policy Study Group, Petitioner	)
v.	)
Federal Energy Regulatory Commission, Respondent	)
Vermont Department of Public Service, Intervenors	)

Consolidated with Nos. 98-1111, 98-1142 and 98-1147

FINAL BRIEF FOR THE PUBLIC SERVICE COMMISSIONS OF NEW YORK, ARKANSAS AND FLORIDA, THE NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS, THE PUBLIC UTILITY COMMISSIONS OF IDAHO, NORTH CAROLINA, AND WYOMING, THE NEW JERSEY BOARD OF PUBLIC UTILITIES, THE VIRGINIA CORPORATION COMMISSION, THE WASHINGTON

UTILITIES AND TRANSPORTATION COMMISSION, THE VERMONT DEPARTMENT OF PUBLIC SERVICE, THE NATIONAL ASSOCIATION OF UTILITY CONSUMER ADVOCATES AND THE OHIO CONSUMER COUNSEL.

[pp. 1-20]

[1]

I. STATEMENT OF THE ISSUES[2] AND STATUTORY PROVISIONS

1. Did FERC exceed its jurisdiction when it claimed authority to preempt the states' regulation of all unbundled transmission of electricity, including the unbundled intrastate transmission of electricity to retail customers?

[2]

The answer is yes.

2. Did FERC exceed its jurisdiction when it claimed authority to determine the rate treatment of all utility costs initially incurred to provide retail electric service, but subsequently "stranded" as a result of competitive access to utility systems or a municipality's formation of a public electric utility?

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[2]This brief relies on the Petitioners' Joint Statement of the Jurisdiction and the Case for a Statement as to jurisdiction and course of proceedings as well as the statement of facts, as supplemented herein.

The answer is yes.

3. Did FERC exceed its jurisdiction when it claimed exclusive authority over regulation of facilities used in local distribution of electricity to customers who will resell the electricity to end-users?

The answer is yes.

The applicable statutes and regulations are included in a separate addendum.

II. SUPPLEMENTAL STATEMENT OF THE CASE

1. The Transmission/Distribution Distinction

The provision of electric service involves the generation of electricity and then either (i) its transmission and local distribution to the ultimate consumer (retail sale) or (ii) its transmission to a reseller (a wholesale sale), which then transmits and distributes the power to an ultimate consumer (a retail sale). Vertically integrated utilities typically generate electricity at central stations, transmit the electricity over long distances and then distribute electricity to the end-user **[3]** over local distribution lines, typically on radial systems at reduced voltages.

The key distinction between transmission facilities and local distribution facilities is that local distribution facilities normally provide one-way power to serve end-users. Power typically flows into a local distribution facility without re-entering the transmission system, i.e., power does not flow

from a local distribution system to other such systems. A transmission system usually ends at a substation where transformers reduce power voltages to lower levels for local distribution.

The bulk of a utility's system is generation and local distribution plant. Using New York as an example, approximately 15% of electric utility revenues support transmission plant; the remaining revenues support local distribution and generation plant.

2. The Wholesale/Retail Split

Traditionally, electric utilities generated, transmitted, and distributed electricity to their customers by way of their own facilities. These sales are called "bundled" sales because the customer pays a single rate for the commodity and its delivery. As indicated, utilities may also sell electricity at wholesale to another utility, which then resells the power to ultimate consumers on its facilities. Therefore, the same utility facilities are used for both wholesale and retail sales.

[4]

State commissions have traditionally regulated all aspects of bundled retail transactions, including service issues and intrastate sale and distribution of electricity.[3] Traditionally, FERC has regulated wholesale power sales and interstate transmission of electricity, which represent a small percentage of the total use of electric systems.

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[3]The states also regulate the generation of electricity.

3. FERC'S Orders -- Matters Challenged

In the orders under review, FERC has attempted to assert jurisdiction over retail sales, when those sales are unbundled into charges for delivery and electricity. FERC concluded that "open access" gave it jurisdiction over rates for transmission of unbundled electricity for retail sales.[4] Order 888, 1991-1996 FERC Regulations and Preambles (hereinafter Stats. & Regs.) ¶31,036 at 31,980 (J.A. 349).[5] FERC also held that if a wholesale sale of energy makes use of a local distribution system, FERC acquired authority over the local distribution facilities **[5]** used for that sale. FERC Order 888-B, 81 FERC 61, 248 at 62, 098 (J.A. 1074).

Finally, FERC asserted that it has authority over "retail stranded costs," arising from a customer's choice of a new electric supplier, because of its claimed authority over unbundled retail transmission. Recognizing, however, that states had authority over the same retail stranded costs, FERC declined to exercise its purported authority. It concluded that

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[4]FERC thus assumed that it had broader jurisdiction over the wheeling of unbundled electricity than it did over the sale of bundled electricity, and expanded its jurisdiction from 1% of utility revenues (wholesale bulk transmission) to as much as approximately 15% of total utility revenues (i.e., all transmission).

[5]FERC stated that while the states retained jurisdiction over the retail sale of the unbundled power after unbundling, it acquired jurisdiction over the unbundled transmission of that power, formerly part of the bundled retail sale. Order 888, FERC Stats. & Regs. at 31,781-82 (J.A. 150-51); Order 888-A, III FERC Stats. & Regs. ¶ 31,048 at 30,180 (J.A. 663), 30, 339-41 (J.A. 822-24).

unless the state regulatory authority lacked power under state law to address retail stranded costs there was no need for its intervention. Order 888, FERC Stats. & Regs. ¶ 31,036 at 31,825 (J.A. 194); FERC Order 888-A, III FERC Stats. & Regs. at 30,182, 30,417-419 (J.A. 898-900).

FERC further asserted jurisdiction over those utility costs that became stranded by retail customers becoming wholesale customers, for instance, through the formation of municipal electric utilities or the expansion of existing ones.[6] It reasoned such costs would not have been stranded "but for" its decision to order open access to utility transmission facilities. FERC Order 888, FERC Stats. & Regs. at 31, 818-19. FERC Order 888-A, III FERC Stats. & Regs. at 30,404. FERC stated that it would be the primary decision-maker and have the final word on **[6]** recovery of those costs. FERC Order 888-A, III FERC Stats. & Regs. at 40,405.

SUMMARY OF ARGUMENT

Congress enacted the Federal Power Act (FPA Act) in 1935 to close a gap in regulation created by a Supreme Court decision that states could not set rates for wholesale energy sold across state lines. Public Utilities Comm'n of Rhode Island v. Attleboro Steam and Electric Co., 273 U.S. 83, 89 (1927). In closing the "Attleboro Gap," Congress preserved

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[6]An entity that had previously been served by an investor-owned electric utility could decide to municipalize, form its own municipal electric utility, become a wholesale customer, purchase bulk power from the wholesale market, and resell power to its inhabitants. In that case, certain utility costs incurred to serve the area (such as installed generating capacity) could be stranded.

the states' jurisdiction over intrastate retail transmission of electricity. In fact, the FPA expressly shielded state regulation of all retail sales and local distribution systems from FERC jurisdiction. FPA §201(b). In the Energy Policy Act of 1992 (EPAct), Congress reiterated the limitation of FERC's jurisdiction to wholesale transactions.

FERC's assertion of jurisdiction over unbundled retail transactions misreads the FPA's plain language, ignores its legislative history, and misapplies precedent.[7] FERC's attempt to regulate the rate treatment of both retail stranded costs and retail-turned-wholesale stranded costs unlawfully intrudes upon the states' exclusive jurisdiction over retail services and rates.

[7]

Finally, FERC's claim of jurisdiction over wholesale distribution ignores the language and purpose of the FPA, which preserves state authority over the transport of power on local distribution systems.

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[7]The Federal Power Commission (FPC) acknowledged to Congress in 1947 that its jurisdiction did not include "the regulation of rates and service outside of [the Attleboro Gap]." A Bill to Amend Section 201 of the Federal Power Act, Hearings Before Subcommittee on Interstate and Foreign Commerce, 80th Cong., 1st Sess., (hereinafter "1947 Hearings"), at 506 (States' Legislative Appendix "A") . FERC's position today, however, is that the same statutory language the FPC described in 1947 as not preempting state regulation now gives FERC jurisdiction over the transmission of electricity to retail customers.

FERC's position is shown in Attachment A. The States' position is reflected in Attachment B.

POINT I[8]

CONGRESS PRESERVED THE STATES' LONGSTANDING JURISDICTION OVER THE REGULATION OF INTRASTATE RETAIL TRANSMISSION

The Act does not define "transmission" for retail purposes, presumably because customers in 1935 did not pay separate rates for the generation, transmission and distribution of electricity. A full reading of the Act, however, together with its legislative history and the Attleboro case that engendered it, shows that the 1935 Congress preserved the states' longstanding authority over retail intrastate service. Such a reading shows Congress intended that: (1) the regulation of retail transactions be left with the states (1947 Hearings at 547-548) ; and (2) that all solely intrastate transactions be subject to state, not federal, jurisdiction.

[8]

A. In Filling The Attleboro Gap, Congress Did Not Diminish The States' Jurisdiction Over Retail Transactions

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[8]The Arkansas Public Service Commission does not join in this point.

1. Congress Reserved To The States Jurisdiction Over Intrastate Service

Under Section 201(a), 16 U.S.C. § 824(a), FERC may regulate the transmission of electric energy only if the energy is "consumed," or used, in a state other than that in which it was initially transmitted, and if the transmission, is not "subject to regulation by the States."[9] Notwithstanding this statutory constraint, FERC has concluded that "open access" would give it jurisdiction over the transmission of unbundled electricity for retail sales.[10] FERC Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966 (J.A. 335). FERC's attempt to regulate the transmission of energy for all unbundled retail sales conflicts with the express limitation of FERC's authority. Under the FPA, the states have regulated the transmission of retail energy sales for over 60 years.

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[9]The Act applies to transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce . . . . such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States," 16 U.S.C. §824(a) (emphasis added). "Electric energy shall be held to be transmitted in interstate commerce if transmitted from a state and consumed at any point outside thereof . . ." 16 U.S.C. §824(a) .

[10]FERC has thus assumed that it has broader jurisdiction over the wheeling of unbundled electricity than it had over the sale of bundled electricity, and has expanded its jurisdiction from 1% of utility revenues (wholesale bulk transmission) to as much as approximately 15% of total utility revenues (i.e., all transmission).

[9]

FERC argues that its limited jurisdiction over the transmission of certain electricity encompasses retail transactions because Congress did not expressly limit its jurisdiction to wholesale transmissions. Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966-67 (J.A. 335-36). Given that "the existence of federal authority to act should appear affirmatively and not rest on inference alone" (Connecticut Light & Power v. Fed. Power Comm'n, 324 U.S. 515, 532 (1945), quoting Yonkers v. U.S., 320 U.S. 685, 692 (1944)), and FERC's inference countermands the Act's safeguarding of state jurisdiction over "local distribution" and facilities used "only for the transmission of electric energy in intrastate commerce," (16 U.S.C. § 824(b)), Order 888 thereby violates the Act's plain language.[11] See Cities of Batavia, Naperville, Rock Falls et al. v. F.E.R.C., 672 F.2d 64, 68, n.2 (D.C. Cir. 1982) [wherein this Court upheld FERC's decision that it lacked jurisdiction over retail rates under 16 U.S.C. section 824j].[12]

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[11]"(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but . . . shall not apply to any other sale of electric energy . . ." 16 U.S.C. section 824(b) (emphasis added).

[12]In 1935, most electric facilities were intrastate facilities (Hearings on H.R. 5423, House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess., [hereafter "1935 Hearings"] at 413 and 763). Thus, states' rights advocates in Congress added the "intrastate" clause to the FPA "so that [the Act] specifically will not apply to intrastate business." New York Times,

[10]

2. The Courts and FERC. Itself Have Recognized That Congress' Goal Was To Fill The "Attleboro GAD" Which Had Left Wholesale Transmission Unregulated

The genesis of the Federal Power Act was the Supreme Court decision in Attleboro that state regulation of interstate wholesale sales would burden interstate commerce. 273 U.S. at 89. In the absence of federal regulation, however, that decision meant no regulation of interstate sales whatsoever. Congress filled this "Attleboro Gap" by empowering the FPC to regulate wholesale electricity rates.[13]

June 8, 1935, "Utility Foes Map Floor Fight, 1935 Hearings, Testimony of John E. Benton, General Sollcitor, NARUC, at 748, 763 et seq.

[13]Dozier DeVane, Solicitor of the Federal Power Commission, stated to the House Committee on Interstate and Foreign Commerce that: "... [S]ection 201 is intended to give the Federal Power Commission jurisdiction over the wholesale rates only. (1935 Hearings at 497) ... [T]he plan of this bill with reference to the regulation of rates [is that] it seeks to leave in the state commissions the power to regulate retail rates but through some federal agency assist the state commissions making available to them the proper data for the determination of those rates. Id. at 520. To the same effect, H.R. Report No. 1318, 74th Cong., 1st Sess., at 8, "the [Federal Power] Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce" (emphasis added).

But the Act was not a preemption statute; indeed, it preserved state authority in retail matters. The Supreme Court has emphasized that the specific language of FPA section 201(b) expressed Congress' intent to draw a "bright line" easily ascertainable between state and federal jurisdiction:

> What Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale 'at wholesale to local distributing companies' and allowed state regulation of a sale 'at local retail rates to ultimate consumers.' [citation omitted].

[11]

This conclusion has been consistently reaffirmed in subsequent cases. In Panhandle Eastern Pipeline Co. v. Public Service Commission of Ind., 332 U.S. 507, which considered the reach of §l(b) of the Natural Gas Act, the Court said that 'the line of the statute was thus clear and complete. It cut sharply and cleanly between sales for resale and direct sales for consumptive uses. No exceptions were made in either category for particular uses, quantities or otherwise.'

Fed. Power Comm'n v. Southern California Edison, 376 U.S 205, 214, 215 (1964), citations omitted (emphasis added). In the ensuing years, the states have regulated all aspects of electric service to retail customers, as Congress intended.

FERC based its claim here to preempt state regulation of transmission to retail customers on Fed. Power Comm'n v. Florida Power & Light, 404 U.S. 453 (1972), reh'g denied, 405 U.S. 948 and Jersey Central Power & Light v. Federal Power Comm'n, 319 U.S 61(1943). Those cases, however,

were "purely factual" disputes (Florida Power & Light at 463)[14] and uphold FERC's accounting authority over public utilities connected to an interstate grid. Indeed FERC's brief to the Supreme Court expressly disavowed any intention to seek jurisdiction over retail sales. As FERC (FPC) stressed:

> [F]inally, and most important, the Commission's rate jurisdiction over interstate **[12]** sales was limited to sales at wholesale; no authority over retail sales was granted.

FPC Brief on Writ of Certiori to the U.S. Supreme Court, October Term, 1970 at 20, 21 (emphasis added); see FPC v. Southern Cal. Edison, 376 U.S. 205, supra. Thus, FERC cannot now point to Florida Power & Light and Jersey Central as a basis for preempting state jurisdiction over retail transmission.

FERC's position here also conflicts with its longstanding view that the FPA need not be amended to clarify its protection of State authority. In 1947, the FPC stated "in the regulation of rates and service, the definitions [in the Act] have been so drawn to plug and no more the Attleboro gap." 1947 Hearings at 527. And in response to an amendment, proposed in 1967, after the 5th Circuit's decision in Florida Power & Light (discussed supra), the FPC testified that such an amendment was "unwarranted" because "the

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[14]See Carstens, Friends of the Earth, et al. v. N.R.C., 742 F.2d 1546, 1557 (D.C. Cir. 1984) [citing Florida Power & Light for the proposition that when a court considers "a purely factual question within [its] area of competence" the court should defer to the agency.") The issue here is a question of law.

accounting situation (such as the one in Florida Power & Light) differs from rate jurisdiction, where the states regulate retail sales and the FPC regulates wholesales" See 1967 Hearings, Testimony of Hon. Lee C. White, Chairman, Federal Power Commission, at 121, 123, 125.[15]

[13]

3. In 1992 Congress Reiterated That States Would Regulate All Retail Deliveries of Electricity

While expanding FERC's authority to order wholesale wheeling, Congress in 1992 reiterated that FERC could not preempt state regulation of retail wheeling of electricity. 16 U.S.C. §824k. EPAct states: "Nothing in this subsection [giving FERC authority over wholesale wheeling] shall affect any authority of any State or local government under State law concerning the transmission of electric energy directly to an

[15]Notwithstanding its prior assurances to Congress, FERC Order 888 states that "to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service are subject to the exclusive jurisdiction of the Commission" (Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,966 (J.A. 335)).

ultimate consumer" 16 U.S.C. §824k(h) (emphasis added).[16] The legislative history confirms that:

> "the vast majority of the activities of the electric utility industry are subject to state public utility commission jurisdiction, and that has not been changed by this legislation, . . . (Congressional Record, October 8, 1992, at S. 34013). This [act] manifests Congressional intent to continue to limit the FERC's authority to wholesale transactions only, Id. at 34015 (emphasis added) . . . the FERC's authority is strictly limited to transmission services provided for the delivery of bulk power supplies to legitimate wholesale customers" Id. at 34018 (emphasis added).

(emphasis added).

FERC Order 888 misreads EPAct as merely prohibiting FERC from ordering retail wheeling, impliedly assigning FERC jurisdiction over retail wheeling rates. There is no language in **[14]** EPAct that even remotely suggests that although Congress prohibited FERC from ordering retail wheeling, it intended FERC to preempt the states' jurisdiction over retail wheeling rates contrary to FERC's conclusion in

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[16]EPAct should, of course, be read in concert with the 1935 Act. See Imazio Nursery, Inc. v. Greenhouses, 69 F.3d 1560, 1564 (Fed. Cir. 1995) ["It is an elementary rule of construction that all parts of an act relating to the same subject should be considered together . . ."].

Order 888, FERC Stats. & Regs. at 31,781 (J.A. 150). Rather, EPAct gave FERC jurisdiction to order wholesale wheeling on a case-by-case basis, and preserved the states' authority over retail transactions.[17]

4. The Unbundling Of Transmission Rates Does Not Transfer The States' Jurisdiction Over Intrastate Retail Sales To FERC

Nothing in the FPA or its legislative history implies that unbundling a retail sale would exclude the intrastate transportation component of that sale from state jurisdiction, leaving the states with control over only the commodity. The underlying transaction remains an intrastate transmission of energy to retail customers, which is the part of the transaction directly affecting customers that Congress left with the states. 16 U.S.C. §824(b)-(c) . See Arkansas Elec. Coop. Corp. v. Arkansas Public Service Comm'n, 461 U.S. 375, 394 (1983)

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[17]FERC stated that its primary purpose for issuing FERC Order 888 and its progeny is "to remedy undue discrimination in the provision of interstate transmission services by public utilities." FERC Order 888-A, III FERC Stats. & Regs. at 30,175 (J.A. 658) . It presents no evidence, however, that discrimination has taken place, and it has not even attempted to show why state commissions are incapable of preventing such discrimination at the retail level. See Congressional Record, October 8, 1992, Discussion of Senator Wallop (R-Wy), at S. 34014. FERC can address alleged discriminatory denial of transmission access in wholesale sales or in wholesale transmission rates sales. FERC's dramatic seizure of power over unbundled retail transmission, however, is not supported by any Congressional goal of preventing discrimination.

[15] [["a]lthough AECC is tied into an interstate grid, its basic operation consists of supplying power from generating facilities located within the State to member cooperatives, all of which are located within the State"].

FERC's reading of the EPAct, if adopted, would also impede Congress' goal of encouraging competition in the electricity market. See Energy Policy Act of 1992, Pub. L. No. 102-486, 1992 U.S.C.C.A.N (102 Stat.) 1961-1962. Under FERC's theory, states that advanced Congress' will by unbundling retail tariffs would suffer diminished jurisdiction, while states that did not unbundle, and thereby impeded competition, would avoid preemption.[18]

United Distribution Companies v. Federal Energy Regulatory Comm'n, 88 F.3d 1105, 1153 (1996), cert. denied, 117 S. Ct. 1723 (1997), cited by FERC to support its contrary claim (FERC Order 888-A, III FERC Stats. & Regs.

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[18]FERC's decision on retail transmission gives rise to a variety of transmission arrangements. For instance, (1) an end-user could choose bundled service, which FERC agrees is fully subject to state regulation; or (2) an end-user could purchase electricity from a "reseller" of energy that is the wholesale customer for the unbundled transmission service; finally, (3) an end-user could piece together its own package of services by purchasing unbundled transmission service from a utility and purchasing energy from a wholesaler, either from out-of-state (3a), where it would be an unbundled retail transmission in interstate commerce, or in-state (3b) when it would be an unbundled retail transmission in intrastate commerce.

at 30,336 (J.A. 819), does not do so. Among other distinctions, United Distribution addressed only interstate gas transportation. 88 F.3d at 1153. ["FERC retains jurisdiction over the interstate transmission component of a retail sale" (emphasis added)]. Indeed, this Court **[16]** distinguished its holding giving FERC jurisdiction over interstate transportation from those "interstate pipelines that receive natural gas at their state boundary that is consumed within the state and subject to state commission regulation." United Distribution, 88 F.3d at 1153, n.62.

5. FERC's Jurisdictional Arguments Do Not Warrant Deference

Because Congress has spoken directly to the matter at issue, FERC's construction of its statute is entitled to no special deference:

> If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency must give effect to the unambiguously expressed intent of Congress. Chevron U.S.A.v. Natural Resources Defense Council, Inc., 467 U.S. 837, 842-43 (1984).

In sections 201(a), 201(b) and 212(h) of the Federal Power Act, Congress preserved state power over retail sales. Moreover, defining retail jurisdiction does not require application of FERC's technical expertise (Compare, Elec. Indus. Ass'n Consumer Elecs. Group v. FCC, 636 F.2d 689, 695 (D.C. Cir. 1980)); nor do the general provisions of the FPA delegate to FERC oversight over the complexities of the

entire electric industry (Compare, Dept of Health and Human Services v. Fed. Labor Relations Auth., 976 F.2d 1049 (D.C. Cir. 1992)).

Even if Congressional intent were unclear, FERC's construction would not deserve deference because, where a federal agency attempts to preempt areas traditionally regulated by the **[17]** states, the Court "start[s] with the assumption that the historic police powers of the States were not to be superseded unless that was the clear and manifest purpose of Congress." Hillsborough County v. Automated Medical Laboratories, Inc., 105 S. Ct. 2371, 2376 (1985).

Further, FERC's assertion of jurisdiction over retail transmission is unsupported by statutory language or history, which abound in contrary statements. Chevron U.S.A.v. Natural Resources Defense Council, Inc., 467 U.S. 843 (1984); Southeastern Michigan Gas Co. v. FERC, 133 F.3d 34, 43 (D.C. Cir. 1998). The FPC itself stated that: "The important task of the regulation of consumers' rates is left entirely to the States. 1935 Hearings, Testimony of FPC Commissioner Clyde Seavey at 384 (emphasis added); see New York Times, March 8, 1935, "Rayburn Bill Held No Blow To States". Although Congress, in 1935, could not contemplate a competitive, unbundled market, it clearly relied on the FPA's precise assignment of state jurisdiction, which "carefully preserved the States' essential regulatory authority over matters of local import," and did "not assign to the Commission any authority over retail rates." 1967 Hearings at 124 (emphasis added).

B. FERC Regulation of Intrastate Retail Transmission Would Be Unwieldy And Detrimental To Electric Customers

1. FERC Regulation Would Be Infeasible

Ratemaking entails a delicate balancing of interests (e.g., Duquesne Light Co. v. Barasch, 488 U.S. 299 (1989)), particularly with respect to retail rate regulation, which **[18]** involves numerous, diverse customers. When asked in 1947 whether the federal government was better equipped than the states to regulate retail rates and services the FPC's Assistant General Counsel stated, "I definitely say, No" (1947 Hearings at 575). single federal agency simply cannot balance ratepayer and shareholder interests for hundreds of companies nationwide.

2. The States Are Better Equipped To Regulate Customer Service

The development and enforcement of retail service standards also requires sensitivity to local conditions that only state commissions can provide. Overly stringent standards can drive up costs and deter economic growth, while insufficient safeguards can endanger customers' safety and welfare.[19]

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[19]For example, FERC has made it clear that it does not intend to apply gross negligence standards commonly applied by states in assessing a utility's liability for service failures. American Elec. Power Serv. Corp, et al, 78 F.E.R.C. ¶61,070 at n. 28 (1997); New York State Elec. & Gas Corp., 79 F.E.R.C. ¶61,371

Under FERC's approach, it would be required to handle retail customer complaints about transmission service from all over the country. The States are in a far superior position to handle customer service problems and protect the rights of small retail consumers.

Beyond that, the advent of retail access enables millions of retail electric customers to contract with alternative **[19]** providers of transmission service. Inevitably, these customers will encounter service, billing and other difficulties. State organizations that have long dealt with similar problems will be able to deal with those issues when they arise in an unbundled environment. FERC lacks any capability to handle complaints of retail customers, yet its approach would require it to do just that.

3. FERC Preemption Could Undermine The Reliability Of Electric Service

Reliability standards for electric service, and the costs that should be incurred to meet them, must be addressed on a local level based on local system conditions. These issues defy a one-size-fits-all analysis.

(1997), 1997 FERC Lexis 1244 at 16, n.15. These state "gross negligence" standards have been upheld by state courts (see, e.g., Food Pageant v. Consolidated Edison Co., 54 N.Y.2d 167, 172 (1981); San Dieqo Gas & Elec. Co. v. Superior Ct. of Orange County, 13 Cal. 4th 893, 917 (1996); Garrison v. Pacific Northwestern, 45 Ore. App. 523, 526 (1980)). Holding utilities to an ordinary negligence standard could raise their costs dramatically, a trade-off best assessed by state agencies.

Additionally, FERC's open access provisions conflict with state provisions for energy balancing, dispute resolution, customer security deposit requirements, consumer complaints, and credit worthiness requirements for receiving service. See, Consolidated Edison Co. of N.Y., Open Access Transmission Tariff, Docket No. ER98-1631-000 and ER 98-270-000 [wherein Con Edison has requested waivers from FERC for such requirements]. While FERC has deferred to the states on some of these issues, it nonetheless claims the last word on various intrastate matters reserved by Congress to the states. Additionally, FERC's Open Access provisions cannot realistically be applied to retail service, so utilities and state commissions have been forced to seek FERC waivers on a variety of issues pertaining to retail access.

[20]

The states have more of the information needed to determine the level of reliability required to maintain customer satisfaction and economic health and to respond to system emergencies. It is not feasible for a federal agency to become familiar with the intricacies of local system design and the needs of the many disparate areas within each of the contiguous 48 states. The tendency to develop a one-size-fits-all approach based solely on national goals could be ruinous to local service reliability.

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B. -FERC's Theory For Preempting State Jurisdiction Over Local Distribution Facilities Is Baseless

1. FERC's Theory Conflicts With Its Identification Of Facilities As Local Distribution

FERC created a jurisdictional test consisting of seven indicators to be applied in determining whether a facility is "local distribution," and hence beyond its jurisdiction.[33] If FERC's criteria establish that a facility is a local distribution facility, then the facility and the transport of energy on it are exempt from FERC's jurisdiction as a matter of law, even though the transactions occurring on it are wholesale transactions.

Case law (as FERC itself recognized in Order 888)[34] exempts local distribution facilities from federal jurisdiction and requires that before FERC can assert jurisdiction over such facilities, it must first make a factual determination that they are not local distribution facilities.

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[33]FERC Order 888, FERC Stats. & Regs. at 31,770-71 (J.A. 139-40), 31,780-83 (J.A. 149-52) .

[34]FERC Order 888, FERC Stats. & Regs. at 31,783, n. 546 (J.A. 152).

> Whether facilities are used in local distribution -- although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test (citation omitted) -involves a question of fact to be decided by the FPC as an original matter. Federal Power **[31]** Commission v. Southern California Edison Co., 376 U.S. 205, at 210, n.6 (1964).

This holding, by which FERC itself was "particularly persuaded,"[35] makes no distinction between bundled and unbundled sales. The seven-indicator test established in FERC Order 888[36] represents FERC's current judgment as to what constitutes local distribution, and should be applied in all instances to define the local distribution facilities subject to state regulation rather than federal.[37]

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[35]Order 888, FERC Stats. & Regs. at 31,783 (J.A. 152), n. 546.

[36]FERC Order 888, FERC Stats. & Regs. at 31,770-71 (J.A. 139-40), 31,780-83 (J.A. 149-52).

[37]In Connecticut Power & Light v. Federal Power Comm'n, 324 U.S. 515 (1945), the Court first expressed the need to limit the corresponding potential reach of federal jurisdiction and then discussed the need for enforcing the local distribution facilities exemption in order to reconcile the claims of federal and local governments.

In Arkansas Power & Light v. Federal Power Comm'n, 368 F.2d 376 (8th Cir. 1966), the Commission argued that

FERC ignores its own factual determination when it claims jurisdiction over any facility transporting energy for **[32]** resale.[38] It apparently reasoned that, because wholesale sales of energy, by definition, do not occur on local distribution facilities, such sales must therefore transform a facility that would otherwise be "local distribution" into a FERC-jurisdictional facility. This reasoning is illogical, however; clearly, the function of a facility does not depend on whether a wholesaler decides that title to energy will pass to

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inasmuch as there were wholesale sales for resale, the nature of the lines was irrelevant. The Court noted that, although the Commission stated that evidence concerning the nature of the lines was not relevant, it had made a factual finding as to local distribution and thereby complied with Federal Power Comm'n v. Southern California Edison Co., 376 U.S. 205, at 210 n. 6, infra.

[38]FERC cites Wisconsin-Michigan Power Co. v. Federal Power Comm'n, 197 F.2d 472 (7th Cir. 1952), in its discussion of jurisdiction over wholesale distribution. Order 888, FERC Stats. & Regs. ¶31,036, Appendix G at 31,914 (J.A. 283). That case, however, stands for the proposition that FERC lacks jurisdiction over facilities that it finds to be "local distribution." The Court determined that sales to wholesalers for resale were not made over facilities used in local distribution because the facilities employed were not located at points on the system where local distribution starts and is carried. The court noted that jurisdiction over local distribution of electric energy is reserved to the states and the authority of the states to fix local rates is not disturbed, even in those cases where the energy is brought in from another state. 197 F.2d at 476.

a reseller at a retail customer's meter or path at some upstream point, such as a utility substation.

FERC offers no reasoned analysis of why local distribution should be defined differently for wholesale sales and retail sales; its decision to attempt such a differentiation without such analysis and explanation should be rejected as arbitrary. Transactive Corp. v. United States, 91 F.3d 232 (D.C. Cir. 1996).

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[p. 1]

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A Primer on Electric Power Flow for Economists and Utility Planners

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[2-6]
Resistance and Ohm's Law

Since power is dissipated in a circuit, some force that is opposed to the flow of current must be at work. The example of a locomotive is analogous in some respects. In a frictionless, gravitation-free world, once the initial inertia had been overcome and the locomotive had been given momentum, the locomotive would continue indefinitely its motion at a constant speed without further work being required. But in the real world, power must be applied continually to compensate for frictional forces opposing the direction of motion in order to maintain the locomotive's speed.

A similar problem arises within a conductor. The electrical analogue to file coefficient of friction is *resistance* (symbol *R)*. The resistance of a conductor is a measure of its opposition to current flow; it is a physical property that varies with the conductor's shape, temperature, and other factors. The unit of resistance is the *ohm* (usually signified by the upper case Greek letter omega, Ω).[8] Certain resistance in a conductor can be understood by regarding resistance as being file result of electron-atom "collisions" within the conductor.[9]

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[8]Named for German physicist George Simon Ohm (1787-1854).

[9]Technically, the electrons and conductor atoms do not collide like billard balls, but the movement of the electrons is deflected in a fashion similar to collisions by the electrical fields

When current flow is increased, more collisions occur and more power is dissipated. The resistance of a copper wire is halved when its cross-sectional area is doubled because fewer electron-atom collisions will occur in a thicker wire. A wire with twice the length will also have twice as many collisions and therefore twice the resistance.

> A good conductor allows electrons to flow easily, but they do not necessarily flow fast. The average electron drift velocity is equal to the current per cross-sectional area of a wire divided by the electron density. Algebraically: $v = i/(Ad)$. Applying this formula we discover, perhaps **[2-7]** surprisingly, that the speed of electrons in a current-carrying conductor is very low. In copper there are roughly 1.38×1024 free electrons per cubic inch; a #14 AWG copper wire (which is about 1/16 inch in diameter) has a cross-sectional area of 3.23×10^{3} square inches. For a current of ten Amperes the electron drift velocity is only v = 0.000356 meters per second, or 1.28 meters per hour![10] Of course, an immense nmnber of electrons is moving at this lethargic pace. Moreover, the electric impulses (voltage propagation) associated with these electron movements travel at nearly the speed of light,

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surrounding the electrons of the conductor atoms.

[10] 1.28 m/h = [10C/s]·[1/3.238x10^{-3} in^2]·[1in^{3}1.38x10^{24}electrons]·[0.254m/inch]·[1 electron/1.602x10^{-19}C]

$c = 2.978 \times 10^8$ meters per second. Each electron's movement induces a sequence of movements in other electrons downstream in the wire, with the result being current (or power) that propagates at an enormous speed.

Good conductors have small values for R. A measure of the lack of opposition to current in a conductor, *conductance,* is the reciprocal of the resistance of the conductor: $G = 1/R$. The SI unit of conductance (G) is the *siemens* (S) or the mho.[11]

A *resistor* is a circuit element flint has a known resistance. Electronic circuits often include numerous resistors of different sizes. Their combined effect can be determined using the following rules of combination for resistors:

[Diagram omitted]

The effective resistance of n resistors in *series* (placed sequentially in a single path) is the sum of their individual resistances:

$$R_{total} = R_1 + R_2 + \ldots + R_n.$$

[Diagram omitted]

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[11]The siemens is named for British engineer Sir William Siemens (1823-1883).

The effective conductance of *n* resistors in *parallel* (placed side by side, creating alternative paths) is the sum of their individual conductances:

$$G_{total} = G_1 + G_2 + \ldots + G_n,$$

or equivalently,

$$1/R_{total} = 1/R_1 + 1/R_2 + \ldots +$$

Note that this R_{total} will be smaller than any of the individual parallel resistances.

Individual conductors have a fairly constant resistance under normal operating conditions.[12]

[Diagram omitted]

[2-8]

Ohm's Law states that the current through a conductor is directly proportional to the applied voltage, where the proportionality constant is the conductance of that conductor: $I = EG = E/R$. One ohm is defined as the resistance that permits a current of one ampere to flow when a potential difference of one volt is applied across the resistance: $1\Omega = (1\ V)/1\ \Lambda$. One way to think of resistance, current, and voltage is to compare a resistor to a hole in a leaky balloon. The air

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[12]For the purposes of this chapter, conductors will be treated as idealized, having no resistance, while circuit elements will be treated as having a constant *R* that does not vary with conditions of use. In practice, temperature can affect the resistance of both conductors and electronic components.

in a balloon will escape faster (increased current) if the hole is widened (reduced resistance). Another way to increase the rate of escape is to increase the pressure differential (increased voltage) between the gas inside the balloon and the gas outside the balloon.

As stated previously, voltage is the ratio of power to current ($E = P/I$). Multiplying both sides of this equation by I yields $P = EI$, so the power dissipated by a circuit is the product of the voltage and the current. Substituting $I = E/R$ from Ohm's Law into the power equation shows that $P = E \cdot (E/R) = E^2/R$. Alternatively, substitution of Ohm's Law in the form $E = IR$ yields $P = IR \cdot I = I^2R$. Thus for a circuit with resistance R, power dissipation increases as the square of voltage or current, e.g. doubling file applied voltage doubles the current but quadruples the power dissipation.

The above rules on combining resistances imply that if a voltage is applied to resistors in series, the current through each of the resistors will be the same, $I = E/R_{total}$. If the resistors are in parallel, each resistor of a different size will have its own corresponding current, but the total current will be $I_{total} = E \cdot G_{total}$.

Kirchhoff's Laws

Almost any interesting circuit consists of several paths serving several kinds of devices. Kirchoff's Laws define physical constraints governing how power or current will flow in any network with several paths:

- *Kirchhoff's Current Law* (KCL) states that the sum of the currents entering a point in an electric circuit must

equal the sum of the currents leaving that point. Equivalently, the net current into and out of any point must be zero.

[2-9]

- *Kirchhoff's Voltage Law* (KVL) states that in any closed electric circuit, the sum of the voltage drops across the circuit elements must equal the sum of the applied emf's around every closed loop.

With the use of these laws, the flows on a simple circuit can be predicted. The circuit at right [diagram omitted] includes a direct voltage source (12 V battery), a resistive load (a lamp rated 3 W at 12 V), a switch, and a few conductors (wires) linking these components in series. The resistance of the wires and internal resistance of the battery can be ignored since they are very small compared to the resistance of the lamp.

When the switch is open, there is no path through which the current may flow. Closing the switch creates a path. KVL states that the net voltage around the closed loop must be zero. Since the battery is providing 12 volts, the *voltage drop* across the resistor must also be 12 volts. That is, the potential difference between points A and B is 12 V, but between B and C it is zero. The amount of current that flows can be determined with the voltage-defining equation E = P/I. The lamp draws 3 W at 12 V, so the current flow

$$I = P/E = (3\text{W})/(12\text{ V}) = 0.25\text{ A}.$$

The lamp is a special kind of resistor, the resistance of which can be deduced from Ohm's Law:

$$R = E/I = (12\ \text{V})/(0.25\ \text{A}) = 48\Omega.$$

Adding another 48Ω lamp in series to the existing circuit elements will alter the circuit in several respects. The direct voltage source still provides 12 V, but the total resistance is doubled, to 96 Ω, since series resistance is additive. The entire supply current flows through both of the resistors (lamps) but is now smaller:

[Diagram omitted]

$$I = E/R_{total} = (12\ \text{V})/(96\ \Omega) = 0.125\ \text{A}.$$

The voltage (drop) across the original lamp is now half as large:

$$E = IR = (0.125\ \text{A})(48\ \Omega) = 6\ \text{V}.$$

[2-10]

We could have used Kirchoff's Laws to establish these results: By KVL, the voltage drop across the two lamps must add up to 12 volts. Since the two have the same resistance value, the voltage drop across each must be the same, i.e. 6 volts. By KCL, the current flowing in the loop must be the same as the current flying across each resistor:

$$I = E/R = (6\ \text{V})/(48\ \Omega) = 0.125\ \text{A}$$

Total power dissipated with two lamps in series is:

$$P = EI = (12\ \text{V})(0.125\ \text{A}) = 1.5\ \text{W},$$

versus 3 W with only one lamp. Thus less light is enjoyed than would have been produced by one lamp alone.

[Diagram omitted]

Placing the second 48 Ω lamp in parallel instead of in series produces a different result. Total conductance is additive for parallel resistors, so

$$\begin{aligned} G_{total} &= 1/(1/R_1 + 1/R_2) \\ &= 1/(1/48 + 1/48) = 1/24 \text{ siemens} \end{aligned}$$

The effective resistance of the two lamps in combination is therefore

$$R_{total} = 1/G_{total} = 24\ \Omega,$$

one-half of the resistance of either lamp by itself. By KVL, the voltage across each lamp is the same and equal to the source emf, 12 V, so the current through the original lamp is

$$I_1 = E \bullet G_1 = 12\ \text{V})/(48\ \Omega) = 0.25\text{A}.$$

Since G_2 is the same as G_1, I_2 also equal 0.25 A. By KCL the total current supplied by the battery is:

$$I = I_1 + I_2 = 0.25\ \text{A} + 0.25\ \text{A} = 0.5\ \text{A}.$$

Total power dissipation in the form of light is now $P = EI =$ (12 V)(0.5 A) = 6 W, twice as much as with one lamp alone (so now our battery will not last as long).

Thus we see that the number and location of circuit elements has a critical effect on the currents, voltages, and power dissipation in the circuit. In this example, adding the second lamp will either halve or double the total power dissipation in the circuit, depending on whether the new lamp is installed in series or parallel. Accordingly, for any planned circuit, the designer must anticipate that both of Kirchoff's Laws will hold when choosing the location of circuit elements.

KCL is true because electrons are never destroyed or created at any point in the circuit. KVL is a consequence of the fact that current always flows through a circuit in a fashion **[2-11]** that minimizes power consumption (I^2R losses). To demonstrate this connection to minimal power losses, consider the following circuit:

Power dissipation $P = I_1^2R_1 + I_2^2R_2$

$= I^2R_1 + (I - I_1)^2 R_2$

$= I_1^2R_1 + I^2R_2 - 2II_1R_2 + I_1^2R_2$

P is now a function of I having a minimum where

$$dP/dI = 2IR_1 - 2IR_2 + 2I_1R_2 = 0$$

$$IR_1 = (I - I_1)R_2 = I_2R_2$$

which is KVL for the closed loop ABCD.

[Diagram omitted]

* * * * *

[3-1]

Chapter 3

Structure of Utility Systems

In the previous chapter, the behavior of electricity in a variety of devices was explored. A number of rules were introduced, chiefly in the form of equations, to make possible the analysis of any circuit. In this chapter, some of the ways in which electric utility networks differ from the simple networks of the previous chapter are explained.

- Electric utilities produce power in generators that rotate electric magnets within a frame housing three equally spaced conducting coils, resulting in three distinct "phases" of electricity that differ in timing from each other by 120°. This "3-phase generation" results in considerable capital and operating economies in transmitting power by reducing the number of conductors and the power losses in each. The algebra for determining the combined effects of the three phases depends on whether they are connected in an arrangement that resembles either the letter Y or a triangle, called a "wye" or "delta" arrangement respectively.

- Numerous transformers are used throughout a utility system to increase voltages for efficient transmission and to decrease them to safe and practical levels for distribution subsystems and end-use devices. For transmission planning and control purposes a local

distribution subsystem can be modeled as a single lumped impedance in parallel with the transmission system.

- Transmission lines have their own impedances that must be taken into account by system planners. In particular, the conductors of a transmission line are inherently inductive especially when heavily loaded, which causes them to absorb reactive power. Reactive power must be supplied to the network in order to offset the inductance of the lines and of certain end-use loads such as industrial motors. This can be produced by generators and transmitted but it is of'ten more economically provided at the site of the reactive load.

  Such reactive power "compensation" is desirable because it reduces the amount of current required to deliver a given mount of real power, and it improves voltage control. It is provided by reactive elements added in parallel (shunt) or series to the transmission lines. A shunt capacitor supplies reactive power while a series inductor **[3-2]** consumes it. Compensation can be either passive (fixed) or active (variable in response to system conditions).

- When power demand changes or system resources are lost due to unplanned disturbances, generator output levels must be adjusted almost instantaneously to keep from over- or under-loading circuits. Conservation of energy dictates that an increase in the electric energy delivered to the loads will cause the kinetic energy (frequency) of the generator turbines to decrease.

Changes in the system frequency as well as in tie-line flows for contractual power exchanges with other utilities can be monitored and used to trigger adjustments to the steam injection into the turbines as needed to restore equilibrium and economical operations. For small changes in load, such adjustments occur in real time under the control of electronic telemetry and feedback mechanisms called Automatic Generation Control. Large changes in load or system status must be anticipated and handled with human intervention.

- Several terms and measurements are used to describe a utility system's ability to accommodate changes in power demand or supply availability. "Reliability" is measured by the probability of loss of service to consumers due to unplanned disturbances to system resources, especially unplanned outages of generating units. Reliability is improved by having redundant generation and transmission capacity and by interconnection with other, adjacent utilities. "Security" refers to the ability of the system to accommodate redirected power flows resulting from a sudden loss (e.g. due to lightning) of the transmission circuit between pairs of buses. "Stability" concerns whether generators will remain in synchronization with each other as they jointly respond to changes in system status. Operating transmission and generation resources below their theoretical capacity limits generally improves security and stability.

* * * * *

[3-12]
Transmission and Distribution

Figure 3.1 on the next page is a schematic representation of how generation, transmission and distribution resources are configured in a utility system. At the source of electric power, different kinds of energy (kinetic, chemical, nuclear) are converted into electric energy in a three-phase generator producing power at around 15,000 volts. Transformers then step up this voltage to a few hundred thousand volts at a *bus* to the transmission line. A bus is any location where electrical devices have interconnected inputs and outputs. There are buses at the junctions of transmission lines with generators, transformers, other transmission lines and distribution subsystems.

Three-phase transmission lines carry low current, high voltage power through isolated areas, using three or four cables (depending on whether the neutral line is present or not). Typically, voltages of 69,000 Volts or above are deemed transmission level, while conductors operating at or below 13,000 Volts are usually accounted for as part of the distribution system. Near the distribution areas a step-down transformer (substation) decreases the voltage and adds the neutral line that is used in the provision of the single-phase power to consumers. Different types of loads use a different number of phases to **[3-13]** meet their power and voltage needs. Three-phase motors take advantage of the constant instantaneous three-phase power, while resistive devices like stoves and light bulbs use line or phase voltage, according to the size of their requirements.

[Diagram omitted]

The transmission system is electrically isolated from the structure and performance of the distribution systems by step-down substation transformers. For transmission planning purposes this means that regional distribution-level loads can be aggregated and regarded as the effects of a single impedance. Operationally, this electrical isolation makes each distribution region relatively immune to the effects of disturbances in other regions, e.g. when lightning knocks out a distribution line. Changes in the end-use load requirements are conveyed back to the transmission system by the substation transformer through changes in current. An increase in power demand at the customer loads causes an increase in the distribution level current flint induces a corresponding change in the current level on the transmission side of the transformer. These current variations will cause the generators to deliver more or less power as needed, through feedback mechanisms explained below.

Not shown in Figure 3.1 are the important components for transmission system monitoring and protection, such as circuit breakers, capacitor banks, and the system operating center. In addition, this figure depicts only a single path from one generator to the load(s). Any real utility includes several generators interconnected to loads in more of a web-like geometry, with multiple paths on which the power will flow. By virtue of Kirchoff's Laws, power arriving at any bus will distribute itself in part to each of the other circuit paths going out of that bus, in inverse proportion to their respective impedances. This phenomenon is referred to as *loop flow;* it has the consequence that power cannot be directed to flow along specific circuits, e.g. just those owned by a particular

utility or those that happen to be operating at below their rated capacity. Loop flows can become a financial and operating problem when power spreads out over lines not owned by the parties scheduling a power transfer.

Control of Generators

It is critical that generation facilities be able to respond essentially instantaneously to the shifting patterns of electric load and that the transmission system have enough flow capacity and controllable voltage support (reactive power compensation) to serve a wide **[3-14]** range of demand requirements. Much of this control must be automatic, relying on feedback from the system itself to guide the corrective actions. Two indicators of system status are primarily relied upon for much of this *Automatic Generation Control (AGC):* system frequency and tie-line flows.[8]

Contract terms and regulatory requirements, and practical engineering considerations require a utility to provide electric power within a very narrow range of frequencies. Even modest deviation can cause severe damage to generators and to electric equipment designed specifically for 60 cycles per second. Steam turbines in particular are vulnerable to fatigue and cracking if operated away from 60 Hz by as little as $\pm$ 0.05 Hz for even a few minutes. A fully loaded steam turbine may be able to sustain 58 Hz for no

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[8]Voltages are also closely monitored in order to protect system stability, but frequency and tie-line changes are the primary barometers for maintaining the economic operation of the system. See Chapter 5 for a fuller discussion of stability.

more than ten minutes cumulatively over its entire operating life.[9]

When the mechanical torque on the turbines (due to the steam or other prime mover) is exactly equal to the opposing electrical torque (arising from the counter-emf in the loops of the generator), the frequency of rotation will be a constant. However, when the power demand changes so that it no longer equals power supplied, the rate of rotation of the generator(s) will automatically increase or decrease as dictated by conservation of energy. For instance, when the load increases, the electrical torque exceeds the mechanical torque, causing the frequency of rotation (hence of the supplied alternating current) throughout the system to decline. More prime mover energy (water flow, steam, etc.) must be supplied to one or more generators to balance the increased power demand. A mechanism on each load-following generator called the *governor* manages these changes in energy input whenever the frequency change exceeds a narrow "deadband" range. A gas-fired peaking plant will have a narrower deadband and a faster response than a baseload coal plant, so the peaking plant will respond first to any short-term variations in load. By adjusting the responsiveness of these generators (called the *droop),* the desired sharing of responsibility across several generators for load changes can be pre-programmed into the system. As will be explained

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[9]To protect the system and its customers, load shedding is scheduled to occur in the MAIN NERC region in 10% blocks, whenever frequency drops to 59.3, 59.0, and 58.7Hz. See Stambach and Ewart, EPRI EL-6360-L, 1989 for a discussion of frequency tolerances and for operating procedures to manage transmission system dynamics.

further below, this adjustment actually involves two phases. **[3-15]** First the plants' mechanical power is matched to the electrical power demanded, usually in a matter of two to ten seconds. This will not occur at 60 Hz but, at a slightly lower frequency when meeting increased demand. Second, the governor *setpoints* are gradually adjusted over a few minutes to move the system back to 60 Hz. Within certain limits, these adjustments can be done in a fashion that achieves an economic dispatch order among the participating plants.

One very important concern for transmission planners and system operators is maintaining system *stability* at or very near 60 Hz as multiple generators adjust to accommodate a new demand or supply condition. The governor mechanisms cannot usually cause an immediate, direct restoration of the system frequency. Instead, the momentum built up in the turbines when they initially respond to increased loading causes them to overshoot the 60 Hz target a bit. Provided they do not overshoot by too much, the electric torque will act as a brake on the generators and induce a reverse correction. Ideally, these oscillations quickly dampen out and converge on 60 Hz for all generators on the system. If they do not, and the generators fall out of synchronization with each other, voltage variations throughout the system can become erratic and extreme, creating unintended power flows that trigger rapid protective shutdown of overloaded circuits. Again by conservation of energy, this sends very strong feedback signals to the generators, occasionally creating a very

complex problem that results in widespread *voltage collapse*.[10] Thus it is critical that system frequency be tightly controlled.

Most utilities are interconnected with several of their neighboring utilities. This linkage affords considerable capital and operating economies, largely because of economies of scope and the related benefits of risk diversification. With a larger network, more alternative paths are available for moving power to each demand node. With more generators interconnected, the probability of unplanned plant outages flint comprise a significant portion of total load is greatly reduced, so generation capacity reserve margins **[3-16]** per MW of peak load can be lower for a given target level of *reliability*. (Reliability is often measured by the probability that plant outages will make it infeasible to serve the entire power demand. Utilities usually maintain sufficient generation and transmission capacity reserves that this is a very unlikely possibility). The total load of an interconnected system itself is somewhat more stable than that of an individual utility because of imperfect correlation of demand across the large

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[10]While protracted metropolitan blackouts due to voltage collapse are fairly rare, collapses lasting a few seconds to a minute have occurred roughly once annually throughout the developed world every year since 1970. Most recently (12/14/94), an outage at a 345 kV substation i Idaho (and possibly other events) triggered a cascading outage that affected ten states and British Columbia, causing the WSCC interconnected system to separate into four islands. The power was restored in most areas within a few minutes, though some were out for a few hours. See NERC, August 1991, for a survey of the causes of and planning procedures for coping with this risk, and Electric Utility Week (12/19/94) for details on the WSCC event.

pool of end-users. This allows better utilization of baseload plants to capture their operating economies of scale. All of these pooling benefits improve system reliability and decrease capital and operating costs. In order to manage how such benefits are shared, the interconnected utilities must control the *tie-lineflows* between themselves at their borders. Tie-line flow measurement and management are the second important means of achieving economic performance goals for the transmission and generation system.

Operationally, interconnected or "pooled" utilities are usually managed as several *control areas,* within each of which there is a sufficient number of generators to follow load and to control system frequency and tie-line exchanges. The fie-lines between control areas are used for contractual power flows under pooled dispatch (economy interchange), wheeling arrangements, bulk power sales from one utility to another, and unplanned flows that occur when one utility suddenly needs the slack generation capacity of another for rectifying an emergency condition. Any change from scheduled tie-line flows becomes the basis for centrally controlled (pool level) corrective action (primarily to the generators) in order to assure that one utility does not inadvertently supply replacement power to another without compensation. The adjustments to restore planned fie-line flows are not necessarily the same as those that would restore the system frequency. Such changes in flows or system frequency are called *area control errors* (ACE). The ACE is measured every few seconds at each control area. It is given by:

$$ACE_j = \text{average frequency in control area}_j \bullet \text{bias}_j + \text{net unscheduled tieline flows into or out of area j}$$

The *bias* term captures how many MWs of local generation are typically required to offset a 0.01 Hz frequency shift. This ACE is measured in MW, and it will roughly equal the mount of generation shortfall in a given control area. Because of the governor controls described above, an imbalance in area j may be first met by a load-following unit outside of area j. This will be reflected in ACE_j as a frequency decline and a net scheduled import, while the area(s) supplying the new demand (or replacing the lost supply) in j will measure **[3-17]** a frequency decline and a net export. Exports have the opposite sign of imports, so these ACE measurements will be approximately zero outside of area j. This reveals which area needs to make adjustments, without having to evaluate the state of each and every supply or demand bus within each control area. The AGC system adjusts the setpoints of the governors on plants flint are participating in load-following and frequency regulation to restore each ACE to zero. Tiffs also brings frequency back to 60 Hz.[11]

Computers and electronic telemetry equipment are used to make these kinds of system observations and to help the system controller to maintain economic dispatch of the generators for modest changes in load. These computers are

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[11]In fact, restoring ACE to zero may not cause frequency to equal precisely 60 Hz, in part because of inaccuracies in estimating control area biases. As a result, utilities may find that a system clock gains or loses a small amount of time over the course of a day, indicating that some inadvertent interchange has occurred. This is generally corrected in kind with subsequent MWs rather than monetary payments. See Wood and Wallenberg, 1984, pp. 291-354, for a discussion of AGC and interchange management.

based at control area centers, of which there were 154 in the U.S. as of 1993.

For large changes in load, such as might arise unexpectedly due to a forced outage or a lighting strike that disables a portion of the transmission network, human anticipation and astute, timely operator intervention are required. The primary defense against such contingencies is to maintain buffers of reserve generation and transmission capacities sufficient to absorb the most severe potential disruptions to the system. A system capable of automatically adapting to any single contingent disruption, i.e. of adjusting without further loss of lines or loads to a new supply-demand balance at 60 Hz, is said to be *secure*.

The design of unbundled electric power services and open access protocols must be sensitive to the fact that generation operations mid transmission control are intimately related. The boundary between the two functions is not a precise one. Generators sometimes have to be adjusted to protect the transmission system, and transmission transactions such as wheeling obligations may alter the security of network operations. Analytically, determining how many MW of transmission flow capacity reserves are required for security and how generation and wheeling can be scheduled to achieve a pattern of power flows consistent with the needed transmission reserve margins requires modeling techniques like those described in the next chapter.

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